Supreme Court, U.S.
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In the Supreme Court of the United States

SHELL PETROLEUM INC., AND
SUBSIDIARY CORPORATIONS,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

ON PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether collateral estoppel bars a party from litigating a federal tax case involving different tax years and separable facts from a prior case, in contravention of the "separable facts" doctrine of *Commissioner v. Sunnen*, 333 U.S. 591 (1948).

2. Whether collateral estoppel can bar a party from litigating for the first time issues that were not necessary to the determination of a prior case on the ground that the prior court made statements regarding those issues that were part of "the analysis that formed the basis for" the prior court's decision.

RULE 29.6 STATEMENT

Pursuant to Supreme Court Rule 29.6, petitioner identifies the following parent corporations and publicly held companies that own 10% or more of petitioner's stock: Shell Petroleum N.V. owns 100% of Shell Petroleum Inc.; Royal Dutch Petroleum Company owns 60% of Shell Petroleum N.V.; and The "Shell" Transport and Trading Company, p.l.c. owns 40% of Shell Petroleum N.V.

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PETITION FOR A WRIT OF CERTIORARI

OPINIONS BELOW

The opinion of the Court of Federal Claims (Pet. App. 28a-47a) is reported at 50 Fed. Cl. 524. The opinion of the court of appeals (Pet. App. 1a-23a) is reported at 319 F.3d 1334.

JURISDICTION

The judgment of the court of appeals was entered on February 13, 2003, and a timely petition for rehearing was denied on May 29, 2003. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

In this case, the lower courts applied the doctrine of collateral estoppel in a manner that deprived Shell of its right to litigate for the first time its entitlement under 26 U.S.C. §29 ("section 29") to over $35,000,000 in tax credits for extremely viscous hydrocarbons that Shell produced from eight separate properties in Southern California during the 1988-1989 tax years.

The section 29 credit was enacted by Congress in 1980 as part of the Crude Oil Windfall Profits Tax Act (COWPTA) to decrease the Nation's dependence on foreign oil by providing a tax incentive for the production of fuels from unconventional domestic resources that were otherwise uneconomical or technologically incapable of production. See S. Rep. No. 96-394, at 87 (1979). The credit is available for, among other things, "oil produced from . . . tar sands." 26

U.S.C. §29(c)(1)(A). The statute, however, does not define oil from "tar sands."

Shell produces oil from several properties that meet the definition of "tar sands" used in the industry and adopted by Congress shortly after the enactment of the section 29 credit — namely, rock containing hydrocarbon with a viscosity exceeding 10,000 centipoises. *See* 30 U.S.C. § 209. In the late 1980s, Shell requested an IRS ruling to confirm that this physical definition applied to section 29, and that Shell's production fell within the definition. The IRS ruled, however, that the credit is governed not by this physical definition of tar sands, but instead by a definition stated in Federal Energy Administration (FEA) Ruling 1976-4:

> "The several rock types that contain an extremely viscous hydrocarbon which is not recoverable in its natural state by conventional oil well production methods including currently used enhanced recovery techniques."

See TAM 8940004 (June 20, 1989). The IRS ruling further stated that the eligibility of Shell's production in a particular case requires a "factual determination." *Id.*

Shell believed that the ruling adopted an incorrect definition for section 29, so it commenced a refund suit in federal district court in Delaware with respect to one of its properties (North Midway Sunset) for the 1983-84 tax years. *See Shell Petroleum, Inc. v. United States*, 996 F. Supp. 361 (D. Del. 1997) (Pet. App. 95a-122a), *aff'd*, 182 F.3d 212 (3d Cir. 1999) ("*Shell I*"). In the district court, Shell argued that the oil qualified for the tar sands credit under the 10,000

centipoises definition, and at a bench trial presented evidence that such was an accepted definition within the industry and should therefore be adopted. *Id.* at 362-363, Pet. App. 97a.

The government, for its part, contended the court should import the definition of tar sands found in FEA Ruling 1976-4. *Id.* at 362, Pet. App. 96a-97a. Furthermore, the government maintained (and Shell and the district court agreed) that Shell was "jurisdictionally precluded" by the variance doctrine from arguing that it met the FEA definition. *Id.* at 363, Pet. App. 97a. Thus, if the court adopted the government's position that the FEA ruling applied, the case would be over and there would be nothing more for the court to decide. *Id.*, Pet. App. 97a.

After the bench trial, the Delaware district court held that the FEA definition controls. The court reasoned that FEA Ruling 1976-4 is "congruous" with the legislature's intent in enacting section 29 "to both encourage the development of new technologies and limit the section 29 credit to crude oil substitutes that could not be obtained using conventional methods." *Id.* at 367-368, Pet. App. 108a-110a. The district court did not stop there, however. It further reasoned that both COWPTA's text and legislative history indicate that whenever a statutory term was left undefined, a definition should be borrowed from FEA rulings and regulations. *Id.* at 368-369, Pet. App. 111a-113a (COWPTA looks to "the regulations and rulings promulgated by the FEA under the EPAA" in order to interpret undefined terms therein). Finally, the court rejected Shell's proffered definition; the court said it contravenes COWPTA in that the same oil could fall within COWPTA's definitions of "tar sands" and "crude oil," which, according to the court, are mutually exclusive. *Id.* at 370, Pet. App. 116a.

The Third Circuit affirmed, emphasizing different points from those made by the district court. *Shell Petroleum, Inc. v. United States*, 182 F.3d 212 (3d Cir. 1999) (Pet. App. 65a-94a). According to the Third Circuit, the FEA definition should be adopted because it is more compatible with Congress' intent to exclude from the section 29 credit oils produced by existing enhanced recovery techniques and to encourage the development of new technologies. *Id.* at 221-224, Pet. App. 84a-89a. In support of the former, the court explained, the terms "tar sands" and "crude oil" are mutually exclusive in the Tax Code; the Tax Code defines oil produced by enhanced recovery techniques listed in 10 C.F.R. 212.78(c)(1980) as "crude oil"; and thus oil produced by such recovery techniques cannot be "tar sands." *Id.*, Pet. App. 84a-89a. For the same reasons, Shell's proposed definition would contradict the legislative goals of section 29, according to the Third Circuit. Finally, the court footnoted that the structure of COWPTA indicates that due regard should be given to rulings under the EPAA when interpreting COWPTA. *Id.* at 224, fn. 21, Pet. App. 93a-94a.

In the wake of that ruling, Shell accepted that the FEA definition applies and pursued this refund suit, under 28 U.S.C. § 1491, in relation to different tax years and different properties produced by different technologies. In this action, Shell seeks an opportunity to argue its interpretation of the FEA ruling and obtain the promised "factual determination" whether its production qualifies for the credit under the FEA definition. That is, in *Shell I* the parties debated the *adoption* of the FEA definition; in *Shell II* the taxpayer seeks to argue the *interpretation* and *application* of the definition. To wit, in the instant action Shell stipulated that the FEA definition applies and sought to be heard on two issues that had not been before the Third Circuit: (1) what the FEA definition means—for example, what do the terms "natural state" and

"currently used enhanced recovery technique" mean; and (2) whether the oil at issue (oil produced in tax years 1988-89 from eight properties, seven of which were not before the Third Circuit) fits the FEA definition. Since the courts in *Shell I* had occasion only to select the applicable definition, these are issues that have never been decided by any court, and they relate to tax years and oil fields that Shell has never before litigated.

With respect to two properties (the McKittrick and Coalinga fields), Shell moved for partial summary judgment based on the undisputed fact that it had tried and failed to produce oil from those properties using the technology available in 1980, but was able to produce oil in later years through use of new technology that previously had been unavailable. The government then cross-moved for summary judgment on all eight fields, arguing that the Third Circuit in *Shell I* had already interpreted Ruling 1976-4, and had already decreed that production from steam techniques could not qualify for the tar sands credit. *See* Def.'s Opp. To S.J. at 3-4 ("[Shell is] precluded by the doctrine of issue preclusion . . . from collaterally attacking the decision made by the Third Circuit in *Shell I* that oil produced through enhanced recovery methods in use in 1980, including two steam injection techniques known as steam soak and steam flood . . . cannot qualify for any credit under section 29."). *But cf.* TAM 8940004 (June 20, 1989) (in a ruling issued to Shell, the IRS implies that steam methods can meet the FEA definition). In reply, Shell challenged the application of collateral estoppel and countered with evidence that the methods used in 1988-89 were not "enhanced recovery methods in use in 1980."

Agreeing with the government's expansive application of collateral estoppel, the Court of Federal Claims denied Shell's motion and granted summary judgment for the government.

Pet. App. 63a-64a. In doing so, the court rejected Shell's reliance on the "separable facts" doctrine enunciated in *Commissioner v. Sunnen*, 333 U.S. 591 (1948), on the ground that such doctrine is no longer good law. Pet. App. 48a-49a. Further, the Court of Federal Claims estopped Shell from contesting a number of issues that the Third Circuit had discussed in dicta and in its reasoning. Specifically, the Court of Federal Claims determined that *Shell I* had already adjudicated that the FEA definition requires the use of a new method; that any type of steam drive and cyclic steam technique is, per se, not a new method; that the term "natural state" in the FEA definition refers to a change in chemical composition; and that the terms "tar sands" and "crude oil" are mutually exclusive of each other. Pet. App. 43a-44a. The court rejected Shell's argument that any statements that went beyond the selection of the correct definition could not have been essential holdings in the case and could not have collateral estoppel effect. Pet. App. 44a. According to the court, these points were "essential rational[es] for holding that the FEA Ruling was the proper definition of tar sands," and as such are just as worthy of preclusion as the Third Circuit's holding itself. Pet. App. 44a. Then, after weighing the summary judgment evidence, the court concluded that Shell's production technology did not satisfy the collaterally established principles. Pet. App. 54a-63a.

A divided panel of the Federal Circuit affirmed, concluding that collateral estoppel precluded Shell "from disputing that hydrocarbons produced by enhanced recovery techniques in use prior to April 2, 1980, are crude oil as opposed to tar sand oil." Pet. App. 2a. Shell argued that cases such as *Commissioner v. Sunnen*, 333 U.S. 591 (1948), dictate a limited application of estoppel in Federal tax cases and that estoppel is limited to the ultimate issue decided in a prior litigation. [Br. Appellant p. 18]. The Federal Circuit

did not address the former and rejected the latter argument, holding that collateral estoppel applies not only to the Third Circuit's adoption of the FEA definition, but also to "the analysis that formed the basis for its adoption of this definition." Pet. App. 8a. Then, based on the collaterally established points, the court affirmed that no material issue of fact existed as to whether any of the production at issue falls within the FEA definition. Pet. App. 13a-15a. In its decision, the majority discussed none of the Supreme Court jurisprudence on the subject of issue preclusion, relying instead on its own circuit court precedent.

Judge Newman dissented, noting that "it cannot be decided, on either summary judgment or collateral estoppel, that the facts and procedures of 1988 and 1989 are the same as those that were before the Third Circuit for 1983 and 1984." Pet. App. 16a. Judge Newman emphasized that this case presents "factual issues with respect to [Shell's] later—developed technology . . . not resolved by the Third Circuit" and that "Shell is entitled to establish the differences of its 1988-89 technology from the steam-based tertiary recovery techniques in general use before April 2, 1980, as the statute contemplates." Pet. App. 20a. Judge Newman also pointed out that "the record well supports" that two of the reservoirs at issue "meet the definition of oil from tar sands . . . as defined by the Federal Energy Agency in 1976." Pet. App. 17a.

REASONS FOR GRANTING THE PETITION

The Court should grant certiorari because issue preclusion is judge-made law that, if improperly applied, can—and in this case does—preclude litigants from having their day in court. This case presents two collateral estoppel issues on which the Court's guidance is needed.

The first issue concerns the "separable facts" doctrine announced by the Court in *Commissioner of Internal Revenue v. Sunnen*, 333 U.S. 591 (1948), which provides that collateral estoppel is inapplicable if two cases involve different tax years and separable facts. In *United States v. Stauffer*, 464 U.S. 165 (1984), the Court repudiated the "separable facts" doctrine with respect to non-tax cases; but it left open whether the doctrine remains good law in tax cases.

As a result of the Court expressly leaving this question open, the lower courts and litigants do not know whether the "separable facts" doctrine is still good law in tax cases. Shell's case is an appropriate opportunity to provide clarification on this important issue, because Shell's facts fall squarely within the doctrine and illustrate how, without the doctrine, a party can lose its right to be heard.

Second, the Court should grant certiorari to clarify whether collateral estoppel applies to dicta and intermediate conclusions, as opposed to ultimate issues only. The courts below adopted the Third Circuit's dicta and reasoning as if they were holdings, and on that basis estopped Shell from litigating issues for the first time. This is at odds with the prevailing view, and is an important question of federal law that has not been, but should be, settled by this Court.

1. The Court should grant certiorari to clarify whether the "separable facts" doctrine is still good law in Federal tax cases.

a. In *Sunnen*, the Court introduced the "separable facts" doctrine, which provides that collateral estoppel is inapplicable if two cases involve different tax years and separable facts.

In *Commissioner of Internal Revenue v. Sunnen*, 333 U.S. 591 (1948) (*Sunnen II*), the taxpayer had patented four types of grinding machines, each of which it licensed under separate contract to a manufacturer. The contracts were executed in 1928, 1931, and two in 1939. *Id.* at 593-594. The four contracts were identical in all material respects and each contract provided that in exchange for the patent, the company would pay royalties to the taxpayer. *Id.* at 594-595. At various times, the taxpayer assigned to his wife the right to receive the royalties under each of these contracts. The assignments were similar in form and substance. *Id.* at 595.

In the earlier case, *Joseph Sunnen*, Board of Tax Appeals, Nos. 64117, 69526, and 74077 (June 29, 1935) (*Sunnen I*), involving taxpayer's 1929-1931 tax years, the IRS claimed that the royalties the wife had received on the 1928 contract were income to the taxpayer, notwithstanding the assignment. The government lost. *Id.* at 596.

In *Sunnen II*, involving taxpayer's 1937-1941 tax years, the IRS claimed that the royalties the wife had received under the 1928 contract, as well as those received under the 1931 and 1939 contracts (which had not been at issue in *Sunnen I*), were income to the taxpayer. The taxpayer argued that the previous decision on the 1929-1931 tax years collaterally

estopped the government from arguing that the royalties at issue in 1937-1941 were income to the taxpayer.

In evaluating the application of collateral estoppel, this Court dealt separately with the royalty payments under the 1928 agreement and the royalty payments under the 1931 and 1939 contracts.

For the royalties paid on the 1931 and 1939 contracts, the Court held collateral estoppel inapplicable on the ground that the later action involved different tax years and "separable facts." *Id.* at 601. According to the Court: "if the relevant facts in the two cases are separable, even though they be similar or identical, collateral estoppel does not govern the legal issues that recur in the second case." *Id.* For this reason, the Court determined, the later action with respect to the 1931 and 1939 contracts is "free from the effects of the collateral estoppel doctrine." *Id.* at 602. The Court reached this conclusion notwithstanding that the 1931 and 1939 contracts were "identical in all important respects" to the 1928 contract. *Id.* at 602.[1]

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[1] The Court cited Dean Griswold's article, "Res Judicata in Federal Tax Cases," 46 Yale L.J. 1320, 1336, which explains there should be no vested rights/disabilities in decisions of law. Such are tantamount to private tax codes and violate a basic tenet of the income tax system—uniform treatment of taxpayers. Different laws could apply to similarly situated taxpayers, that is. To illustrate in the context of the tar sands tax credit, if in a later year not yet litigated Shell and its competitor lease adjacent properties and produce oil that exists in the ground in an asphalt-like state, it ought not be the case that the legal requirements for Shell to qualify for the tax credit are more onerous than the standards applicable to its competitor. *Cf. Anderson, Clayton & Co. v. United States*, 562 F.2d 972, 992 (5th Cir. 1977), *cert. denied*, 436 U.S. 944 (1978)

For the royalties paid on the 1928 contract, the Court determined that since the two cases involved the exact same issue, on the exact same contract, the "separable facts" rationale did not apply. But that did not end the matter. The *Sunnen* Court went on to rule that, even when the facts are identical, collateral estoppel is still inapplicable if there has been an intervening event—something has happened such as a change in legal landscape or in controlling facts—between the time of the first suit and the time of the second suit to warrant relitigation of the issues. *Id.* at 602-604. The Court concluded there had been such a change.

For ease of identity during the discussion that follows, this Petition for Certiorari will refer to the *Sunnen* Court's methodology on the 1931 and 1939 contracts as the "separable facts" doctrine, and will refer to the Court's methodology on the 1928 contract as the "intervening events" doctrine. It is the former doctrine—the "separable facts" doctrine—that is at issue in this case and requires further action by this Court.

b. The Court's decisions in *Stauffer* and *Montana* have created confusion in the lower courts on the extent to which the "separable facts" doctrine remains valid in Federal tax cases.

This Court, in *United States v. Stauffer*, 464 U.S. 165 (1984), ruled that *Sunnen's* separable facts test does not apply to non-tax cases. The Court, however, expressly reserved

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("The most persuasive policy consideration in the present context is that perpetuation of an erroneous tax decision over a number of years would prejudice the losing party and violate the policy of tax uniformity among taxpayers. 18 *Moore's Federal Practice* sec. 0.422(1) (2d ed. 1974).").

judgment on whether it remains in force in Federal tax cases. At footnote 5 the Court states:

> Thus, the Government's argument essentially is that two cases presenting the same legal issue must arise from the very same facts or transaction before an estoppel can be applied. Whatever applicability that interpretation may have in the tax context, see Commissioner v. Sunnen, 333 U.S. 691, 601-602 (1948) (refusing to apply an estoppel when two tax cases presenting the same issue arose from "separable facts"), we reject its general applicability outside of that context.

Since *Stauffer*, courts and litigants have been confused as to whether the "separable facts" doctrine is still valid for Federal tax cases. The Ninth Circuit, for example, has said: "There is conflicting authority in this circuit as to whether *Sunnen*'s separable facts doctrine is still alive. The Supreme Court has rejected the separable facts doctrine in general terms, but has implied that it might have continuing validity in the tax context." *Peck v. Comm'r*, 904 F.2d 525, 527-528 (9th Cir. 1990) (citations omitted); *Carter v. U.S.*, 973 F. 2d 1479, 1483 fn. 1 (9th Cir. 1992). Similarly, the United States Tax Court, a court of national jurisdiction, echoed: "...it is unclear whether the separable facts doctrine [first enunciated in *Commissioner v. Sunnen*, 333 U.S. 591 (1948)] is still good law in the tax context..." *Monahan v. Comm'r*, 109 T.C. 235, 242 (1997).

In particular, the lower courts are uncertain about the impact of this Court's decision in *Montana v. U.S.*, 440 U.S. 147 (1979). A survey of post-*Stauffer* decisions shows that courts are divided on whether *Montana* effectively overruled the "separable facts" doctrine and limited *Sunnen*'s

applicability to the "intervening events" doctrine. *See, e.g.*, *Kamilche Co. v. U.S.*, 53 F. 3d 1059, 1062 n.3 (9th Cir. 1995) (relying on pre-*Stauffer* authority to conclude that *Montana* limited *Sunnen*); *Northern Illinois Gas Co. v. U.S.*, 12 Cl. Ct. 84 (1987), *aff'd*, 833 F.2d 1582 (Fed. Cir. 1987) (same); *cf. North Georgia Elec. Membership Corp. v. City of Calhoun*, 989 F. 2d 429, 433-434 (11th Cir. 1993) (same in non-Federal tax case); but compare *Weiner v. U.S.*, 2002 U.S. Dist. LEXIS 26456 at *19-21 (S.D. Tex. Nov. 20, 2002), and related order 255 F. Supp. 2d 624 (S.D. Tex. 2002) (*Sunnen*'s separable facts test survives *Montana*); *Levitt v. Comm'r*, T.C. Memo 1993-294, 66 T.C.M. (CCH) 40 (1993) (relying on *Sunnen* and the "separable facts" doctrine); *cf. Sabow v. Pennington County*, 500 N.W.2d 257, 260 (S.C. 1993)(same in non-Federal tax case).

Shell submits that *Montana* did not affect application of the "separable facts" doctrine to Federal tax cases and this Court should so clarify—indeed, the Court in *Montana* never even uttered the words "separable facts."

In that case, the State of Montana imposed a gross receipts tax on public contractors but not private contractors. The United States, through a public contractor it had hired for a dam project, filed an action in Montana's state court, contesting the tax as unconstitutional on the ground that it discriminated against the United States. One month later, the United States filed a duplicative action in Federal court, making the exact same arguments, with respect to the same tax periods, on the same project. The complaint was almost verbatim the complaint filed in Montana state court. On request of the parties, the Federal court stayed the action pending the outcome of the state court litigation.

The United States lost in state court and exhausted its appeals to the Montana Supreme Court, which declared the tax statute constitutional. The United States then tried to take another bite at the same apple and filed a motion for summary judgment in the Federal court action that had been stayed pending the outcome of the Montana state court case. The District Court would have no part of it, concluding that the state court decision collaterally estopped the United States from contesting the constitutionality of the tax statute.

This Court affirmed. In doing so, the Court discussed *Sunnen* in relation to only one aspect of its opinion. It reiterated the "intervening events" doctrine in *Sunnen*—that collateral estoppel is inapplicable where there is a change in controlling facts or legal atmosphere—and then rejected the United States' attempt to fit within the doctrine. On that score, the United States argued that the earlier decision was predicated on a factual assumption that did not exist in the later action. The Court determined, however, that the factual difference was immaterial and accordingly the United States could not find shelter under *Sunnen*.

Thus, rather than limiting the doctrines enunciated in *Sunnen*, *Montana* reinforces *Sunnen*'s "intervening events" doctrine. With respect to *Sunnen*'s "separable facts" doctrine, the Court simply had no reason to speak to the issue. The tax periods were the same, the material and operative facts were inseparable, and neither party argued otherwise; nothing in the opinion suggests that by implication the "separable facts" doctrine was affected. *Cf. Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 484 (1989) (lower courts should not infer that Supreme Court decisions have been silently overruled from subsequent decisions, but rather should leave to the Court "the prerogative of overruling its own decisions."). Indeed,

Footnote 5 of *Stauffer*, *supra*, confirms that *Montana*'s silence on the issue did not impact the "separable facts" doctrine.

Nevertheless, in the aftermath of *Montana* and *Stauffer*, the status of the separable facts doctrine remains unsettled. Sometimes the government argues it is alive and well, *e.g.*, *Kamilche Co. v. U.S.*, *supra*, other times, as in this case, it is the taxpayer making that argument and the government taking the contrary position, *e.g.*, *Levitt v. Comm'r*, *supra*.

Certiorari is therefore desirable to end the confusion and to address the question left unanswered by the Court in footnote 5 of *Stauffer*—namely, whether the separable facts doctrine remains good law in Federal tax cases.

c. Shell's case comes squarely within the "separable facts" doctrine as enunciated in *Sunnen* and therefore provides an appropriate opportunity for the Court to settle the validity and scope of the doctrine.

Shell's fact pattern is in all pertinent respects the same as the fact pattern to which this Court applied the "separable facts" doctrine in *Sunnen*.

The first action, *Shell Petroleum, Inc. v. United States*, 182 F.3d 212 (3d Cir. 1999), *aff'g* 996 F. Supp. 361 (D. Del. 1997) (*Shell I*), involved tax years 1983-1984 and arose in the factual context of Shell's oil production from the North Midway Sunset field in Southern California. *Id.* at 363; Pet. App. 71a. The legal issue before the courts in that case was whether the term "tar sands" in section 29 should be defined according to an industry definition or instead by a ruling issued by the Federal Energy Administration. *Id.* at 214; Pet.

App. 66a. The government argued it was the latter and prevailed.

This action, *Shell II*, involves different tax years (Shell's 1988-1989 tax years), different technologies, and different fields than those at issue in *Shell I*. Pet. App. 16a. In *Shell I*, the only oil field at issue was the North Midway Sunset. In *Shell II*, Shell contends that its oil production from seven fields not at issue in *Shell I* (as well as the North Midway Sunset which was at issue in *Shell I*) qualifies for the section 29 credit. Since the tax years of the later action are different and the relevant facts are separable (the oil production is from seven fields not at issue in the earlier case), *Sunnen* controls, provided it is good law.

Accordingly, this case presents a perfect opportunity for this Court to clarify whether litigants in Federal tax cases can rely on the "separable facts" doctrine.

2. The Court should grant certiorari to settle the extent to which collateral estoppel applies not only to the ultimate issues resolved in previous litigation between parties but also to passages in the court's reasoning.

Even if this Court were to determine that *Sunnen*'s "separable facts" doctrine is no longer good law, the Federal Circuit's collateral estoppel holding is still erroneous for reasons that present another important legal question that warrants the attention of this Court.

The Federal Circuit determined that collateral estoppel applies not only to the Third Circuit's adoption of the FEA definition, but also to "the analysis that formed the basis for its adoption of this definition." Pet. App. 8a. The trial court similarly found collateral estoppel applicable to the "analytical

steps used by the Third Circuit in interpreting [section 29]," as these were "essential rationales for holding that the FEA Ruling was the proper definition of tar sands." Pet. App. 44a.

The notion that collateral estoppel applies to the numerous reasons given by the *Shell I* courts to support the ultimate conclusion in that litigation conflicts with numerous lines of authorities and inherently raises thorny questions that will unnecessarily complicate the application of issue preclusion doctrine.

As this Court has suggested, collateral estoppel does not apply to issues considered collaterally or incidentally to deciding an ultimate issue. *See North Carolina Railroad Co. v. Story*, 268 U.S. 288, 294 (1925) ("It is well settled that the principle of res judicata is only applicable to the point adjudged and not to points only *collaterally under consideration*, or incidentally under cognizance or only to be inferred by arguing from the decree.") (emphasis added). Instead, collateral estoppel applies only to the actual "ultimate issues" in the case; that is, issues that have controlling legal significance. *See U.S. v. State of Alaska*, 521 U.S. 1, 14-15 (1997) (statements in a prior decision, while part of the court's reasoning, were not of controlling legal significance; thus collateral estoppel was inapplicable as to those statements).

In other words, collateral estoppel applies only to "issues that were somehow 'ultimate' in the first litigation." Wright & Miller, *Federal Practice & Procedure* § 4421, at 196 (2d ed. 1994); *see also Fife v. Bosely*, 100 F.3d 87, 89 (8th Cir. 1996) (collateral estoppel applicable to ultimate issues that are the same in both cases and not to subsidiary findings); *Minneapolis Community Dev. Agency v. Buchanan*, 268 F.3d

562 (8th Cir. 2001) (Lay, J., dissenting) (collateral estoppel applies only to ultimate issues). The Restatement (Second) of Judgments similarly articulates: "If issues are determined but the judgment is not dependent upon the determinations, relitigation of those issues in a subsequent action between the parties is not precluded." Restatement (Second) of Judgments § 27, cmt h (1980).

Further, the Restatement suggests a way to make these standards easily workable. According to comment h, one way to assess whether the judgment is dependent upon the determinations in question—and hence is an "ultimate" issue —is to inquire whether the determinations could "be the subject of an appeal by the party against whom they were made." *Id.* *See also*, *Warner/Elektra/Atlantic Corp. v. County of DuPage*, 991 F.2d 1280, 1282-1283 (7th Cir. 1993) (collateral estoppel is inapplicable to findings that cannot be appealed).

Under these standards, nothing that the Third Circuit said in *Shell I* about the *meaning* of the FEA definition could have collateral estoppel effect. While the Third Circuit might have had legitimate reason to consider certain interpretative aspects of the FEA ruling, these matters were considered only incidentally on the road to deciding the ultimate issue in the case—which of two definitions applies. Furthermore, Shell could not have appealed the court's statements about the meaning of the FEA definition, or the meaning of terms like "currently used recovery techniques." Prevailing on these disputes on appeal would not have changed the judgment. Given the way the case was framed, with Shell conceding defeat if the FEA definition were adopted, judgment for the government was automatic once the court determined that the FEA definition applied, no matter how that definition might be interpreted.

Furthermore, the proposition that reasoning in an opinion is not "estoppable" draws support from an analogous line of authority that "mediate data" is not entitled to collateral estoppel effect. Judge Learned Hand, in *The Evergreens v. Nunan*, 141 F. 2d 927, 928 (2nd Cir. 1943), *cert. denied*, 323 U.S. 720 (1944), explained that mediate/predicate facts found in the first action are not conclusive as to mediate/predicate facts in the second action. *See also*, *Yates v. U.S.*, 354 U.S. 298, 336-338 (1957); Branscomb, "Collateral Estoppel in Tax Cases: Static and Separable Facts," 37 TEX. L. REV. 584, 595 (1959). Analogously, just as predicate facts should not be accorded collateral estoppel effect, predicate points of law should not either. Collateral estoppel should be limited to issues that were ultimate in the first proceeding and should not extend to points that were collaterally considered—that is, steps taken to reach the ultimate issue or finding.

This should be especially true when the prior decision rests on alternative reasons, as in this case. There is currently a split of authority in the circuits on whether alternative grounds for a decision carry the effect of collateral estoppel. *See C.B. Merchant Co. v. Eastern Foods, Inc.*, 756 F.2d 317, 319 (4th Cir. 1985) (existence of alternative bases for judgment precludes estoppel); *New Jersey Phil. Presbytery v. New Jersey Bd.*, 654 F.2d 868, 876 (3d Cir. 1981) (same); *Comair Rotron, Inc. v. Nippon Densen Corp.*, 49 F.3d 1535, 1538 (Fed. Cir. 1995) (alternative grounds may both be entitled to collateral estoppel). These cases involve multiple ultimate issues—alternative holdings—that support the judgment. There would be even greater complication if courts had to decide not just which holding is entitled to estoppel but also which of the reasons in support of that holding is entitled to estoppel.

The proposition that reasoning should not come within the purview of estoppel, particularly when there are alternative reasons at work, is also consistent with the line of authority that "dicta" is free from the effects of collateral estoppel. *See, e.g., Marlene Indus. Corp. v. NLRB*, 712 F.2d 1011, 1015-1016 (6th Cir. 1983) ("The determination of an issue in an earlier proceeding must be essential to the judgment, it cannot be dicta."); *Thomas v. Cassidy*, 892 F.2d 637, 640-641 (7th Cir. 1990), *cert. denied*, 498 U.S. 812 (1990) (collateral estoppel inapplicable to comments made in previous decision regarding an issue which it did not have jurisdiction to decide).

The Federal Circuit's holding conflicts with the foregoing principles. Shell conceded in *Shell I* that if the Third Circuit applied the Federal Energy Administration definition it could not qualify for the Section 29 tax credit for the North Midway Sunset field for the 1983-84 tax years. *Shell Petroleum, Inc.*, 182 F.3d at 214, Pet. App. 67a ("Shell concedes that it is not entitled to a refund if we accept the DOE Ruling definition."). Shell had made the same concession in the district court. *See Shell Petroleum, Inc.*, 996 F. Supp. at 363, Pet. App. 97a ("The parties agree that if the Court determines that the FEA Ruling definition of 'tar sands' is to be applied when interpreting Section 29, judgment should be entered for the Government."). Thus, the only ultimate issue decided in *Shell I* was the proper source for the definition of tar sands, not its meaning.

The Federal Circuit, nevertheless, extended the application of collateral estoppel to statements made by the Third Circuit concerning the interpretation of the FEA Ruling and statements concerning the court's rationale that the terms "tar sands" and "crude oil" are mutually exclusive, all of which were dicta, or at most analytical steps—intermediate

conclusions—to reach the ultimate and essential issue and holding of the case. In fact, none of the issues on which the Federal Circuit estopped Shell are listed in the *Shell I* pre-trial order. That order delineates all of the issues of fact and law that everyone—the court, the government, and the taxpayer—agreed were to be litigated. Now, Shell comes to discover that *Shell I* was its one and only opportunity to litigate numerous issues not listed in the pre-trial order and issues on which Shell was jurisdictionally precluded.

Such unfair surprise illustrates why dicta and reasoning are not normally within the realm of collateral estoppel and why there is no identity of issues in this case, as is required by *Sunnen*, 333 U.S. at 599 (for collateral estoppel to apply, the issues must be "identical in all respects"), and *Montana*, 440 U.S. at 155 (for collateral estoppel to apply, the issues must be "in substance the same"). Further, as a broader policy matter, giving collateral estoppel effect to passages in reasoning—as the Federal Circuit has done—will make issue preclusion a more prevalent and a more uncertain feature of complex litigation. It may allow litigants to argue about the meanings of reasoning in both trial court and appellate court opinions, and permit courts in later cases to pick and choose among alternative reasons advanced by the courts in earlier cases. Opening the door to such disputes is not conducive to judicial economy, the reason for issue preclusion in the first place.

CONCLUSION

Granting the petition would afford this Court an opportunity to speak on two important issues of judge-made law on which the lower courts are in conflict and, on either ground, to reverse the Federal Circuit's decision and send the case back to the trial court for further proceedings in which

Shell may for the first time have the opportunity to obtain the "factual determination" that the IRS promised it over a decade ago.

The petition for a writ of certiorari should be granted.

Respectfully Submitted,

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APPENDIX A

UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

No. 02-5037

[Filed February 13, 2003]

SHELL PETROLEUM, INC., AND SUBSIDIARY CORPORATIONS, Plaintiff-Appellant,	)
v.	)
UNITED STATES, Defendant-Appellee.	)

Appealed from
United States Court of Federal Claims
Chief Judge Edward J. Damich

JUDGES: Before NEWMAN, RADER, and PROST, Circuit Judges.

OPINION

PROST, Circuit Judge.

Appellants, Shell Petroleum, Inc., and subsidiary corporations ("Shell"), appeal the decision of the United States Court of Federal Claims granting summary judgment to the United States. The court held that Shell was not entitled to a tax refund for calendar years 1988 and 1989 under the Crude Oil Windfall Profits Tax Act ("COWPTA"), Pub. L. No. 96-223, 94 Stat. 229 (1980) (codified in scattered sections of 7, 19, 26, and 42 U.S.C.) (repealed in part 1988), based on a tax credit provided in 26 U.S.C. § 29 (2000) for "oil produced from tar sands" through wells drilled between January 1, 1980, and December 31, 1992. Because we conclude that Shell is precluded from disputing that hydrocarbons produced by enhanced recovery techniques in use prior to April 2, 1980, are crude oil as opposed to tar sand oil under § 29[1], and because there is an absence of evidence that Shell recovered hydrocarbons by any means other than enhanced recovery techniques available in 1980, we affirm.

BACKGROUND

Crude oil is generally extracted through wells from underground reservoir formations of sand or rock containing tiny pore spaces permeated with oil. To be recoverable, the oil must flow through the pore spaces to a well. The extremely viscous hydrocarbons at issue here, however,

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[1] "Tar sand oil" denotes "oil produced from tar sands."

cannot flow through to a well unless their viscosity is reduced. Enhanced recovery techniques[2] recover such oil by reducing the viscosity of the oil through the application of heat, steam or other substances.

For calendar years 1983 and 1984, Shell filed amended tax returns claiming that oil produced from one of its eight reservoirs at issue in this appeal was tar sand oil and it was therefore entitled to a tax credit under § 29. Shell recovered the oil using tertiary recovery methods that were well established and widely accepted in the petroleum industry by 1980. These methods were steam soak, begun in 1963, and steam flood, begun in 1971. The tax credits were denied and Shell timely filed suit in the United States District Court for the District of Delaware, which entered judgment for the United States. *Shell Petrol., Inc. v. United States*, 996 F. Supp. 361 (D. Del. 1997). Shell appealed to the Third Circuit.

The Third Circuit's resolution of the appeal turned on the proper definition of "oil produced from tar sands," which COWPTA did not define. *Shell Petrol., Inc. v. United States*, 182 F.3d 212 (3rd Cir. 1999) ("*Shell I*"). Shell argued the definition of "tar sands" should be based on the "viscosity standard" or "quantitative standard" allegedly commonly accepted by the petroleum industry in 1980. *Id.* The government argued that the court should adopt the definition

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[2] "Tertiary recovery methods," "tertiary enhanced recovery methods," and "enhanced recovery techniques" are the same. *Shell Petrol., Inc. v. United States*, 50 Fed. Cl. 524, 527 n.5 (2001).

contained in Department of Energy Ruling 1976-4, 10 C.F.R. ch. II Rulings 371, 372 (1980) ("DOE ruling" or "DOE definition"). *Shell I*, 182 F.3d at 214. That definition of "tar sands" reads as follows:

> The several rock types that contain an extremely viscous hydrocarbon which is not recoverable in its natural state by conventional oil well production methods including currently used enhanced recovery techniques. The hydrocarbon-bearing rocks are variously known as bitumen-rocks, oil impregnated rocks, oil sands, and rock asphalt.

Synthetic Fuels Processed From Oil Shale, and Coal, 41 Fed. Reg. 25,886 (June 26, 1976) (emphasis added).[3]

After examining the statutory language, structure, legislative history and purposes of COWPTA, the Third Circuit concluded that COWPTA defines oil produced using enhanced extraction techniques available when the § 29 credit was enacted as crude oil, which Congress clearly distinguished from tar sand oil. *Shell I*, 182 F.3d at 217, 221-22. Based on this determination, the Third Circuit held that the definition of "tar sands" most compatible with congressional intent was found in the DOE ruling. *Id.* at 221. The Third Circuit affirmed the denial of the tax credits

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[3] The DOE ruling was issued by the DOE's predecessor, the Federal Energy Agency. By the time COWPTA was enacted, however, the ruling was redesignated a DOE ruling in the Code of Federal Regulations. *Shell I*, 182 F.3d at 214 n.3. The Court of Federal Claims and the parties in the instant case refer to this ruling as the "FEA Ruling."

because Shell did not contest the district court's finding that its oil was produced using tertiary recovery methods widely available in 1980. *Id.* at 223. Therefore, the Third Circuit concluded that Shell's oil was crude oil and could not be tar sand oil warranting tax credits under § 29. *Id.* at 216, 221.

At issue in this case are eight reservoirs containing extremely viscous hydrocarbons from which Shell produced oil during calendar years 1988 and 1989 using enhanced recovery techniques (cyclic steam injection and/or steam drive injection). Shell's tax refund action is based on the same § 29 tax credit that was at issue in *Shell I*. The parties agree that the DOE definition of "tar sands" is controlling in this case and that the phrase "currently used" in that definition means in use on or before April 2, 1980, the date of the enactment of COWPTA. The issue presented to the Court of Federal Claims was the applicability of the DOE definition of "tar sands" to the oil produced by Shell at its eight reservoirs.

Before the court, Shell filed a motion for partial summary judgment with respect to two of the reservoirs contending that the relevant facts demonstrated beyond dispute that the production of oil from these two reservoirs qualified for the § 29 credit. The government subsequently filed a motion for summary judgment contending that, as a matter of law, the tax credit must be denied with respect to all of the subject reservoirs.

The Court of Federal Claims held that Shell was estopped by the Third Circuit's decision in *Shell I* from disputing that hydrocarbons produced by enhanced recovery techniques in use prior to April 2, 1980, are crude oil and not oil produced from tar sands for purposes of the § 29 tax credit. The court

further concluded that Shell failed to raise a genuine issue of material fact with regard to whether Shell used production methods to extract hydrocarbons other than by means of recovery methods that were in commercial use prior to April 2, 1980. The court granted summary judgment in favor of the government after concluding that Shell's oil was not oil produced from tar sands under § 29 because the oil was produced using steam assisted recovery methods that were in commercial use prior to April 2, 1980.[4] The court also denied Shell's motion for partial summary judgment and ordered dismissal of Shell's complaint.

Shell filed a timely appeal and we have jurisdiction pursuant to 28 U.S.C. § 1295(a)(3). On appeal, Shell challenges the application of issue preclusion, the grant of summary judgment to the government, and the denial of its partial summary judgment motion.

DISCUSSION

I.

We review a trial court's application of issue preclusion, also known as collateral estoppel, *de novo*. *Dureiko v. United States*, 209 F.3d 1345, 1355 (Fed. Cir. 2000). Under the doctrine of issue preclusion, "a judgment on the merits in a first suit precludes relitigation in a second suit of issues actually litigated and determined in the first suit." *In re*

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[4] The court granted summary judgment in favor of the government with respect to one of the eight reservoirs because Shell did not reveal the production method for that reservoir.

Freeman, 30 F.3d 1459, 1465 (Fed. Cir. 1994) (citations omitted). Issue preclusion is generally appropriate if: (1) an issue is identical to one decided in the first action; (2) the issue was actually litigated in the first action; (3) the resolution of the issue was essential to a final judgment in the first action; and (4) the party defending against issue preclusion had a full and fair opportunity to litigate the issue in the first action. *Id.*; *Jet, Inc. v. Sewage Aeration Sys.*, 223 F.3d 1360, 1365-66 (Fed. Cir. 2000).

On appeal, Shell argues that the court erred in ruling that *Shell I* precludes it from contesting the government's legal interpretation and proposed application of the DOE definition of "tar sands." According to Shell, the court applied an overly expansive view of issue preclusion thereby depriving it of the opportunity to litigate many issues for the first time. Because in *Shell I* it accepted the government's position that it was jurisdictionally barred from arguing that its production met the DOE definition, Shell maintains that *Shell I* decided no more than which of two proffered definitions of "tar sands" to adopt as governing the § 29 tax credit. Thus, according to Shell, any determinations by the Third Circuit that went beyond the selection of the DOE definition were not necessary to the outcome of the litigation.

The government counters that the Court of Federal Claims correctly concluded that all the requirements of issue preclusion were met. Thus, the government maintains that Shell is estopped from relitigating the issue of whether hydrocarbons produced by enhanced recovery techniques in use prior to April 2, 1980, are crude oil and not oil produced from tar sands. We agree.

The Court of Federal Claims considered the first two requirements of issue preclusion together. These are whether the issue the government seeks to estop Shell from relitigating was raised and litigated in *Shell I*. Shell's limited view of collateral estoppel would require that only the Third Circuit's adoption of the DOE definition of "tar sands" is binding on this court, but not the analysis that formed the basis for its adoption of this definition.

We see no grounds, however, for such parsing of the Third Circuit's conclusions leading to its adoption of the DOE ruling as the proper definition of "tar sands." The question resolved by the Third Circuit was whether the oil Shell produced using enhanced recovery techniques available in 1980 qualified for a § 29 tax credit, a determination that turned on the proper definition of "oil produced from tar sands." *Shell I*, 182 F.3d at 214. The Third Circuit concluded that oil produced by "enhanced recovery techniques" available in 1980 is crude oil and cannot be "oil produced from tar sands." *Id.* at 221-22. This issue was raised and litigated by Shell. *See Banner v. United States*, 238 F.3d 1348, 1354 (Fed. Cir. 2001) (stating that an issue was "actually litigated" because it was properly raised by the pleadings, submitted for determination, and determined (citing Restatement (Second) of Judgments § 27 cmt. d (1980))); *Harris Trust & Sav. Bank v. Ellis*, 810 F.2d 700, 705 (7th Cir. 1987) (stating that "when one party introduces evidence on a dispositive issue of fact, and an adverse party with opportunity and motive to contest the presentation chooses not to, the ensuing finding is entitled to the same respect as one litigated to the hilt"). Although Shell did not contest that oil produced using tertiary recovery methods available in 1980 is crude oil, it argued that the same oil could also be classified

as tar sand oil. *Shell I*, 182 F.3d at 221-22; *Shell Petrol.*, 50 Fed. Cl. at 533, nn.10,11. Based on its interpretation of COWPTA, the Third Circuit rejected these arguments because "Congress clearly distinguished tar sand oil from crude oil." *Shell I*, 182 F.3d at 221. Furthermore, the Third Circuit specifically rejected Shell's definition of "tar sands" because it would classify oil produced from enhanced extraction techniques available in 1980 as tar sand oil. *Id.*

The next issue preclusion requirement is that the resolution of the issue was "necessary to the judgment." In this regard, it is clear that the Third Circuit adopted the DOE definition of "tar sands" precisely because it concluded that hydrocarbons that are produced by means of conventional oil well production methods, including enhanced recovery techniques in use on or before April 2, 1980, are "crude oil" and cannot be "oil produced from tar sands" for purposes of the § 29 tax credit. *See Mother's Rest., Inc. v. Mama's Pizza, Inc.*, 723 F.2d 1566, 1571 (Fed. Cir. 1983) (stating that the purpose of the "necessary to the judgment" requirement is to prevent the incidental or collateral determination of a nonessential issue from precluding reconsideration of that issue in later litigation). Thus, the court's determination that oil produced using "currently used enhanced recovery techniques" is crude oil and not tar sand oil was indeed necessary to the resulting judgment.[5]

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[5] Although the ultimate result of the judgment was that Shell was not entitled to the § 29 tax credit, that result necessarily followed because Shell did not contest that the oil at issue in *Shell I* was oil produced using tertiary recovery methods. *Shell I*, 182 F.3d at 223.

The last issue preclusion requirement is that Shell had a "full and fair opportunity to litigate" the issue in the first action. The relevant factors to consider in determining whether this requirement has been satisfied are: (1) whether there were significant procedural limitations in the prior proceeding; (2) whether the party had an incentive to fully litigate the issue; and (3) whether effective litigation was limited by the nature or relationship of the parties. *Banner*, 238 F.3d at 1354. We conclude that, based on this record, the "full and fair opportunity to litigate" requirement of issue preclusion is met. Shell was fully represented by counsel during *Shell I*, it had a monetary incentive to fully litigate the issue, and effective litigation was not limited in any way. Therefore, we agree with the Court of Federal Claims that Shell is precluded from re-litigating the issue of whether hydrocarbons produced by means of enhanced recovery techniques in use prior to April 2, 1980, are "crude oil" and not "oil produced from tar sands" for purposes of the § 29 tax credit.

II.

Shell further argues on appeal that, notwithstanding whether issue preclusion applies, the Court of Federal Claims nonetheless erred in granting summary judgment to the government because a factual dispute exists as to whether the steam assisted oil recovery methods used at the subject reservoirs constitute "currently used enhanced recovery techniques" as of April 2, 1980, under the DOE definition of "tar sands." We review the trial court's grant of a motion for summary judgment without deference. *Impresa Construzioni Geom. Domenico Garufi v. United States*, 238 F.3d 1324, 1330 (Fed. Cir. 2001). Summary judgment is appropriate

when "there is no genuine issue as to any material fact and . . .the moving party is entitled to a judgment as a matter of law." Court of Federal Claims Rule 56(c).

The Court of Federal Claims determined that "enhanced recovery technique" connotes a production method in and of itself, as opposed to an incremental development or improvement in pre-existing methods of production. Moreover, it accepted the government's definition of a "production method" as a method that moves hydrocarbons in a reservoir to a well bore so they can be lifted to the surface. The court, therefore, granted summary judgment for the government because it concluded that all of the technological improvements demonstrated by Shell are ancillary aides that may make cyclic steam or steam drive injection production processes more efficient and cost effective, but do not actually move hydrocarbons from the reservoir to the surface.

Shell argues that the use of new technology not available in 1980, in conjunction with, and that significantly improves the capabilities of, an existing recovery method to produce previously unrecoverable hydrocarbons can amount to a new recovery "technique" within the meaning of the DOE definition.

In support, Shell contends that a determination that the use of steam automatically disqualifies it from the § 29 tax credit is inconsistent with the text of § 29(b)(5), which provides that a § 29 tax credit for producing oil from tar sands must be reduced by any credit allowed under 26 U.S.C. § 43 with respect to the same project. Section 43 provides a tax credit for costs expended in developing qualified enhanced oil

recovery projects involving the application of a tertiary recovery method, which includes steam injection. *See* 26 U.S.C. § 43(c)(2)(A)(i) (2000). Shell maintains that § 43 is limited to enhanced oil recovery projects, and the recovery methods identified in § 43(c)(2) are not used to recover shale oil, the only other "oil" listed in § 29 as qualifying for the tax credit besides tar sand oil. Therefore, in Shell's view, § 29(b)(5) would be superfluous if it were not possible for a production using steam injection to qualify for a § 29 credit.

Shell also argues that although the production technique it used at the eight subject reservoirs included the injection of steam, the technology critical to the production of the hydrocarbons was very different from the technology widely available as of April 2, 1980. In support, Shell asserts that its technological advances include a new way of injecting steam,[6] the "limited entry completions on steam injectors,"[7] and advanced modeling tools to identify the location of oil, determine where to place the wells and how much steam to introduce. In addition, Shell allegedly developed more sophisticated surveillance tools that allowed it to better monitor the movement of oil and heat within the reservoir and thereby change the operation parameters to optimize

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[6] This new device for injecting steam is called a Steam Quality Utilizing Iso-kinetic Deflection, which distributes steam more efficiently and uniformly in the reservoir.

[7] This technology allowed Shell to flood multiple oil zones simultaneously, accelerating production from individual zones and greatly enhancing the profitability of the reservoir.

production. Shell also made use of advances in drilling, facilities design, and well completion methods.[8]

Lastly, Shell specifically argues that oil produced from two of the subject reservoirs in 1988 and 1989 is "oil produced from tar sands" because the oil could not be economically produced using enhanced recovery techniques in use as of April 2, 1980. Shell alleges that it was able, presumably economically, to recover oil from these two reservoirs in 1988 and 1989 because of the enhancements it had developed by that time to its pre-April 2, 1980, recovery technology.

We conclude that the Court of Federal Claims correctly granted summary judgment to the government. First, in our view, the determination that a steam based recovery cannot qualify for a § 29 tax credit does not render the § 29(b)(5) provision superfluous. Rather, as the court recognized, the offset provision can operate if a taxpayer uses a steam based recovery technique in conjunction with a production technique that was new or had not been combined with a steam based recovery method before April 2, 1980, to produce tar sand oil. Furthermore, we agree with the court's conclusion that the term "recovery technique" in the DOE definition of "tar sands" connotes a production method that moves hydrocarbons in a reservoir to a well bore so they can be lifted to the ground surface. The court's interpretation of

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[8] The well completion methods included advances in well casing design that did not collapse at the high pressure and temperature necessary for production. Shell alleges that this advance directly assisted in the movement of hydrocarbons to the ground surface because oil will not flow through a collapsed well bore.

production method is supported by the June 1979 energy regulations, which describe recovery methods as methods of moving oil from the reservoir to the well bore from which the hydrocarbons may then be pumped to the surface. *See* 10 C.F.R. § 212.78(c) (1979).[9]

Contrary to Shell's assertion, therefore, its technological advancements were not necessary to the production of hydrocarbons because Shell has not demonstrated that its allegedly new technologies changed the pre-April 2, 1980, methods of moving hydrocarbons to the surface from the recovery methods available in 1980. Rather, Shell's method of moving the hydrocarbons was no different from the steam based recovery methods available in 1980, i.e., by injecting steam into the reservoir. Although Shell's technological advances may have made steam injection production more cost effective to use in 1988 and 1989 than it was in 1980, the recovery method was nonetheless in use as of April 2, 1980.

Accordingly, we do not accept Shell's argument that previously uneconomically recoverable oil at two of the subject reservoirs, which is now economical to recover due to technological improvements to a pre-April 2, 1980, recovery method qualifies as tar sand oil. Adopting Shell's position would contradict the purposes of COWPTA as interpreted by the Third Circuit. The Third Circuit found that Congress added the § 29 alternative fuel production tax credit "'to encourage energy conservation and production of alternative

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[9] COWPTA defines a "tertiary recovery method" as one of the methods described in subparagraphs (1) through (9) of § 212.78(c) of the June 1979 energy regulations. *See* 26 U.S.C. § 4993(d)(1)(A) (repealed 1988).

energy sources.'" *Shell I*, 182 F.3d at 224 (citations omitted). In so doing, according to the Third Circuit, Congress explained that these alternative energy sources "'typically involve new technologies'" and the information obtained from the "'initial efforts at producing these [alternative] sources will'" benefit the entire economy. *Id.* (citations omitted). As the Third Circuit recognized, continued use of a widely available means of crude oil production is not an "'initial effort[ ]'" that will stimulate the development of new energy technologies. *Id.* (citations omitted). Improvements to conventional recovery methods available in 1980 that make recovery more cost effective, thereby making production at certain reservoirs economically practicable, is likewise not an initial effort that will stimulate the development of new energy technologies. Therefore, even accepting Shell's factual allegations as true, Shell failed to raise a genuine issue of material fact disputing that it used production methods at any of its eight reservoirs other than by means of "currently used enhanced recovery techniques" as of April 2, 1980.

CONCLUSION

For the foregoing reasons, Shell was properly precluded from disputing that hydrocarbons produced by means of enhanced recovery techniques in use prior to April 2, 1980, are "crude oil" and not "tar sand oil" under § 29. Because Shell failed to provide any facts showing that it produced hydrocarbons using enhanced recovery techniques not available on or before April 2, 1980, we also conclude that the oil produced from Shell's eight reservoirs was not "oil from tar sands" and, therefore, is not entitled to receive the § 29 tax credit. Accordingly, we affirm the grant of summary

judgment to the government and affirm the denial of Shell's motion for partial summary judgment.

AFFIRMED.

CONCURBY: NEWMAN (In Part)

DISSENTBY: NEWMAN (In Part)

DISSENT: NEWMAN, Circuit Judge, concurring in part, dissenting in part.

I agree that Shell is collaterally estopped by the decision of the Third Circuit in *Shell Petroleum, Inc. v. United States*, 182 F.3d 212 (3d Cir. 1999), from relitigating the subject matter there decided. The Third Circuit case related to tax returns for 1983 and 1984, and held that Shell was not entitled
to the Section 29 tax credit for recovery from the Potter Sands reservoir. Shell accepts the definition of tar sands used by the Third Circuit, but argues that even under that definition it has established entitlement to the Section 29 tax credit, at least with respect to the two reservoirs of primary focus in this appeal. The Court of Federal Claims decided the issue on summary judgment, holding that Shell was not entitled to the Section 29 credit for any of the reservoirs. However, it cannot be decided, on either summary judgment or collateral estoppel, that the facts and procedures of 1988 and 1989 are the same as those that were before the Third Circuit for 1983 and 1984. Thus while I agree with the panel majority that Shell is estopped from disputing the applicability of the Federal Energy Agency's 1976 definition of tar sands, I do not share the conclusion that this definition precludes Shell's

argument and entitlement with respect to the technology it used in 1988 and 1989.

A

Shell states, and the record well supports, that the Coalinga-Etchegoin and the McKittrick-Tulare reservoirs meet the definition of oil from tar sands, either as defined by the Federal Energy Agency in 1976 as "extremely viscous hydrocarbon which is not recoverable in its natural state by conventional oil well production methods including currently used enhanced recovery techniques," FEA Ruling 1976-4, 41 Fed. Reg. 25,886 (June 23, 1976), or as defined by the Department of Energy in 1980 as "a hydrocarbonaceous material with a gas-free viscosity, measured at original reservoir temperature, greater than 10,000 centipoise,"[1] the definition in the Combined Hydrocarbon Leasing Act of 1981, 30 U.S.C. § 209, and the Energy Policy Act of 1992, 42 U.S.C. § 13554.

The viscosity of the hydrocarbons in the Coalinga tar sands is reported, as measured by the government, as ranging from 125,000 cp to 600,000 cp; and the viscosity of the hydrocarbons in the McKittrick reservoir is reported as ranging from 27,000 cp to 64,750 cp. Shell recovered hydrocarbons from these reservoirs in 1988 and 1989, using methods not in general use on April 4, 1980, the date set in the Section 29 enactment. These methods are described by

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[1] The viscosity of water is 1 centipoise (cp). The record states that most oil produced in the United States has a viscosity below 8 cp, and 98% of crude oil deposits have a viscosity lower than 1,000 cp.

Shell as (1) advanced modeling tools, including the Vogel modeling method and numerical thermal simulators; (2) sophisticated surveillance methods; (3) advanced drilling and well completion methods, including advanced casing design and sand control; and (4) advanced facility design, including cogeneration and steam distribution.

The Court of Federal Claims seriously over-simplified this complex field, in denigrating these procedures as mere "advanced technology," and not "advanced techniques" as purportedly contemplated by the statute.[2] From this oversimplification the trial court concluded that if known steam procedures were adapted through new technology to recover the hydrocarbon from tar sands, the product became "crude oil" by definition, whatever its viscosity and its previous unrecoverability. This leap of logic is not in accordance with the statute and its legislative purpose, and is based on disputed findings inappropriate to summary judgment.

The statute does not state that only some brand new "technique" can qualify for the tax credit, and it is highly unlikely that Congress so contemplated, for the incentive was

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[2] The statute and its history use both "techniques" and "technologies." For example, the Senate Report on the tax credit legislation states that the alternative energy sources eligible for the Section 29 tax credit would "typically involve new technologies." S. Rep. No. 96-394, at 87 (1979), reprinted in 1990 U.S.C.C.A.N. 410, 496. This Report also stated that the purpose of the tax credit is to "encourage the development of these [shale and tar sand] resources by decreasing the cost of their production" through the tax credit. *Id.*

broad and the need was urgent. I do not here evaluate the technologic modifications and improvements made by Shell, but on the undisputed fact that before 1980 tar sands could not be economically harvested at these sites, it is clear that the question could not be summarily decided adversely to Shell. Nor was the question adequately explored by the trial court, who deemed it barred by collateral estoppel. However, the Third Circuit did not deal with later-developed technology, and did not generate estoppel as to all steam-based extraction technology. Estoppel based on the Third Circuit decision is necessarily limited by the application of the definition of tar sands to the facts relevant to the 1983 and 1984 tax years and the Potter Sands reservoir.

Shell was not permitted to prove its proffered facts, on the ruling by the Court of Federal Claims that because Shell used previously known steam-based procedures along with new technology, there is no way that the statutory requirement can be met. Thus the court ruled that whatever the new technology and the changes and improvements used in 1988 and 1989, any procedure using steam-assisted recovery is an "enhanced recovery technique" available in 1980. On this premise the Court of Federal Claims ruled that all hydrocarbon that is successfully extracted from tar sands with steam-based procedures is "crude oil," and that since the Section 29 tax credit is unavailable for crude oil, it is unavailable for this tar sand extraction.

B

It is not disputed that the products of the Coalinga and McKittrick reservoirs have viscosities starting at 27,000 cp. This is not crude oil by any definition. The record does not

establish that the steam extraction techniques of tertiary recovery as generally used in 1980 were capable of economic recovery of the hydrocarbons in tar sands. Although the government argues that these hydrocarbons could have been recovered using those techniques, hindsight and speculation are not probative evidence, and are insufficient grounds of summary judgment.

The factual issues with respect to the later-developed technology used at Coalinga and McKittrick in 1988 and 1989 were not resolved by the Third Circuit in connection with the 1983 and 1984 Potter Sands tax years. These factual issues were not before the Third Circuit, and are not barred by collateral estoppel. *See Cromwell v. Sac County*, 94 U.S. 351, 356, 24 L. Ed. 195 (1876) ("a point not in litigation in one action cannot be received as conclusively settled in any subsequent action"); *Del Mar Avionics, Inc. v. Quinton Instrument Co.*, 836 F.2d 1320 (Fed. Cir. 1987) (same). These facts could not be found adversely to Shell on summary judgment. Shell is entitled to establish the differences of its 1988-89 technology from the steam-based tertiary recovery techniques in general use before April 2, 1980, as the statute contemplates, and to establish whether the hydrocarbon from these reservoirs could reasonably have been economically recovered using those techniques.

The government argues that if the hydrocarbon became economically extractable from tar sands using steam-based technology, it was no longer oil from tar sands but became crude oil. Shell complains that on this reasoning, after a producer develops an economic method of using steam to extract hydrocarbons from tar sands, the hydrocarbon loses its identity as tar sand product. Indeed, this reasoning denies the

legislative premise that "the term 'crude oil' . . . does not include synthetic petroleum, such as oil from shale or tar sands," set forth in S. Rep. No. 96-394, at 56 (1979), reprinted in 1980 U.S.C.C.A.N. at 465. *See also* H.R. Conf. Rep. No. 96-817, at 114 (1979), reprinted in 1980 U.S.C.C.A.N. 642, 667.

Shell states that it tried and failed to economically extract tar sand oil using the "enhanced production techniques" available using steam in 1980. The Court of Federal Claims deemed it irrelevant that the tar sands could not be extracted using procedures in use in 1980, citing the Third Circuit's reference to "incremental tertiary oil" as not entitled to the credit. However, Shell correctly points out that the list of nine tertiary enhanced recovery techniques contained in the energy regulations, 10 C.F.R. § 212.78, which include "steam drive injection" and "cyclic steam injection," permits variations on steam-based techniques to qualify for the tax credit.

It is a question of material fact as to whether the changes achieved by Shell in steam-based recovery are sufficient to satisfy the statutory purpose. That factual question could not be decided adversely to Shell on summary judgment, for Shell showed on the summary judgment record that the steam drive injection and cyclic steam injection procedures in use in 1980 were inadequate to produce more than an "uneconomic trickle" of recovery from tar sands. Shell's position required development of the evidence, and was not amenable to adverse summary judgment.

C

The government also argues that Shell's oil from these reservoirs "poured" or "flowed," arguing that this cannot be the product of tar sands because it "exists in a liquid phase." Shell agrees that the product of tar sands exists in a liquid phase, for "viscosity is a physical property of all fluids. Solids do not have viscosity." Shell's Proposed Findings of Uncontroverted Fact. The product of tar sands is an "extremely viscous hydrocarbon," the words of the Federal Energy Agency Ruling 1976-4, as adopted by the Third Circuit. *Shell Petroleum*, 182 F.3d at 214. "Viscosity is a measure of a fluid's resistance to flow." *Shell Petroleum*, 182 F.3d at 214 n.1. The argument concerning "flow" is not only scientifically flawed; it is irrelevant.

D

The government further states that all tax benefit statutes must be "strictly construed," and that any doubt must be resolved adversely to the taxpayer. However, that is not an accurate generalization. For example, statutes designed to provide an incentive for private investment have been required to be "construed liberally" in order to achieve their purpose. *See Xerox Corp. v. United States*, 228 Ct. Cl. 406, 656 F.2d 659, 678 (Ct. Cl. 1981) (investment tax credit); *Panhandle Eastern Pipe Line v. United States*, 228 Ct. Cl. 113, 654 F.2d
35, 42 (Ct. Cl. 1981) (investment tax credit).

The government also states that Shell paid windfall profits tax on this oil, arguing that Shell viewed it as crude oil and not as tar sand oil, and cannot take a contrary position in the

courts. Shell responds that the dividing line between crude oil and tar sands oil has not been decided, and that the government had taken conflicting or unclear positions -- as is apparent from this litigation. Shell cannot be faulted or subjected to adverse inferences for paying the tax to the extent that it may have done so.

Summary

The Section 29 tax credit is limited to new investment, that is, to wells and facilities placed in service after 1979. It is undisputed that the purpose of Section 29 was to provide, through tax abatement, an incentive to recovery of hydrocarbons that could not be economically recovered by the procedures then available for crude oil. Although the government insists that the tar sand hydrocarbons for which Shell seeks the Section 29 credit were in fact recoverable through tertiary recovery procedures in general use in 1980, Shell proffered contrary evidence based on its actual attempts to recover tar sand hydrocarbons.

The presence of hydrocarbons in tar sands has been known for decades, without economic procedures for their extraction. The congressional purpose of encouraging the development of this large and undeveloped resource is defeated by the ploy of classifying the oil from tar sands as "crude oil" after the technology to extract it is developed. Shell is entitled to prove that the technology it used in these tar sand reservoirs was not generally available before April 2, 1980, with due attention to economic feasibility. I respectfully dissent from this court's endorsement of the trial court's summary disposition and its premises.

APPENDIX B

UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

No. 02-5037

[Filed May 29, 2003]

SHELL PETROLEUM, INC., AND SUBSIDIARY CORPORATIONS, Plaintiff-Appellant,	)
v.	)
UNITED STATES, Defendant-Appellee.	)

ORDER

A combined petition for panel rehearing and for rehearing en banc having been filed by the APPELLANT, and a response thereto having been invited by the court and filed by the APPELLEE, and the petition for rehearing having been referred to the panel that heard the appeal, and thereafter the petition for rehearing en banc and response having been referred to the circuit judges who are in regular active service,

UPON CONSIDERATION THEREOF, it is

ORDERED that the petition for panel rehearing be, and the same hereby is, DENIED and it is further

ORDERED that the petition for rehearing en banc be, and the same hereby is, DENIED.

The mandate of the court will issue on June 5, 2003.

FOR THE COURT,

/s/_____
Jan Horbaly
Clerk

APPENDIX C

UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

No. 02-5037

[Filed June 5, 2003]

SHELL PETROLEUM, INC., AND SUBSIDIARY CORPORATIONS, Plaintiff-Appellant,	)
v.	)
UNITED STATES, Defendant-Appellee.	)

On Appeal from the
United States Court of Federal Claims
No. 97- CV-945

JUDGMENT

This CAUSE having been heard and considered, it is ORDERED AND ADJUDGED:

AFFIRMED.

ENTERED BY ORDER OF THE COURT

DATED FEB 13 2003 /s/ _____
Jan Horbaly, Clerk

ISSUED AS A MANDATE: June 5, 2003

APPENDIX D

UNITED STATES COURT OF FEDERAL CLAIMS

No. 97-945 T

[Filed October 12, 2001]

SHELL PETROLEUM, INC., and SUBSIDIARY CORPORATIONS, Plaintiff,	)
v.	)
THE UNITED STATES, Defendant.	)

EDWARD J. DAMICH, Judge

OPINION

Presently before the Court are the Plaintiffs' motion for partial summary judgment, filed on November 15, 1999, and the Defendant's motion for summary judgment, filed on May 18, 2000. The Court holds that hydrocarbons produced by means of enhanced recovery techniques in commercial use prior to April 2, 1980 are crude oil under Title I of the Crude Oil Windfall Profits Tax Act and cannot be oil produced from

tar sands for the purpose of the section 29 tax credit for nonconventional fuels.[1] Because the Plaintiffs have failed to show that they did not use enhanced recovery techniques in commercial use prior to April 2, 1980, they cannot demonstrate that the oil that they produced was anything other than crude oil, and they cannot demonstrate that they produced from tar sands from any reservoirs at issue in this case. Therefore, the Defendant's motion for summary judgment is GRANTED and the Plaintiffs' motion for summary judgment is DENIED.

I. Introduction

Pursuant to 26 U.S.C. § 7422 and 28 U.S.C. § 1491, the Plaintiffs seek a refund of federal income tax for taxable calendar years 1988 and 1989 under the Crude Oil Windfall Profits Tax Act ("COWPTA"), Pub. L. 96-223, 94 Stat. 229 (1980), *codified in relevant part at* 26 U.S.C. §§ 4991-4993 (repealed), for oil produced from 8 of its reservoirs which they claim to be "oil produced from tar sands," thereby qualifying for a tax credit for the production of fuel from nonconventional sources under § 29 of COWPTA.[2]

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[1] Unless otherwise indicated, "section" or "§" refers to a section in the Internal Revenue Code of 1954 or 1986 (26 U.S.C.).

[2] § 29. Credit for producing fuel from a non-conventional source

(a) Allowance of credit - There shall be allowed as a credit against the tax imposed by this chapter for the taxable year an amount equal to -

(1) $ 3, multiplied by

(2) the barrel-of-oil equivalent of qualified fuels --

Unfortunately, COWPTA does not define "tar sands." For the purposes of this case, the parties agree that the definition of a tar sand, as found in Federal Energy Agency[3] (FEA) Ruling 1976-4, 10 C.F.R. ch. II Rulings 371, 372 (1980) ("hereinafter FEA Ruling"), should control in this case. The FEA Ruling provides that a tar sand consists of:

> The several rock types that contain an extremely viscous hydrocarbon which is not recoverable in its natural state by conventional oil well production methods including *currently used enhanced recovery techniques*. The hydrocarbon-bearing rocks are

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(A) sold by the taxpayer to an unrelated person during the taxable year, and
(B) the production of which is attributable to the taxpayer.

* * *

(c) Definition of qualified fuels. -- For purposes of this section --
(1) In General. -- The term "qualified fuel" means --
(A) oil produced from shale and tar sands

* * *

(f) Application of Section -- This section shall apply with respect to qualified fuels --
(1) which are
(A) produced from a well drilled after December 31, 1979, and before January 1, 1993

26 U.S.C. § 29 (originally designated under § 44D.)

[3] The Federal Energy Agency was a predecessor to the Department of Energy. *Shell Petroleum, Inc.*, 182 F.3d at 214 n.3.

> variously known as bitumen-rocks, oil impregnated rocks, oil sands and rock asphalt.

Synthetic Fuels Processed From Oil Shale and Tar Sands, 41 Fed. Reg. 25886 (June 26, 1976) (emphasis added). This definition was adopted by another court in a previous lawsuit between the parties. *Shell Petroleum, Inc. v. United States*, 996 F. Supp. 361 (D. Del. 1997), *aff'd*, 182 F.3d 212 (3rd Cir. 1999) ("*Shell I*") (involving taxable years 1982-84 and § 29(a), (c)(1)(A)). The parties disagree, however, about whether the production methods that the Plaintiffs used for the 8 reservoirs in question -- steam drive injection and cyclic steam injection -- are "currently used enhanced recovery techniques" in this definition. (Both parties agree that "currently used" means in use on or before April 2, 1980, the date of the enactment of COWPTA.) Obviously, if the production techniques used by the Plaintiffs at the 8 reservoirs in question are "currently used enhanced recovery techniques," then the oil produced from the reservoirs is not oil produced from tar sands, and it does not qualify for the tax credit.

II. The Plaintiffs Are Estopped From Relitigating The Issue Of Whether Hydrocarbons Produced By Enhanced Recovery Techniques In Use Prior To April 2, 1980, Are Crude Oil And Not Oil Produced From Tar Sands For The Purposes Of The Section 29 Tax Credit.

A. Introduction

Defendant argues that the meaning of "currently used enhanced recovery techniques" has already been decided in

Shell I, such that the Plaintiffs are precluded from relitigating this issue in this Court. The doctrine of issue preclusion, also known as collateral estoppel, is designed to "relieve parties of the cost and vexation of multiple lawsuits, conserve judicial resources, and, by preventing inconsistent decisions, encourage reliance on adjudication." *Allen v. McCurry*, 449 U.S. 90, 94, 66 L. Ed. 2d 308, 101 S. Ct. 411 (1980). *See also Blonder-Tongue Labs., Inc. v. Univ. of Ill. Found.*, 402 U.S. 313, 28 L. Ed. 2d 788, 91 S. Ct. 1434 (1971). Issue preclusion will prevent relitigation where the record shows that: (1) the issue to be precluded in the current action is identical to one decided in an earlier action; (2) the issue was raised and actually litigated in a prior suit; (3) the issue was necessary to the judgment; and (4) the party to be estopped had a full and fair opportunity to litigate the issue in a prior suit. *In re Freeman*, 30 F.3d 1459, 1465 (Fed. Cir. 1994); *Mother's Restaurant v. Mama's Pizza, Inc.*, 723 F.2d 1566, 1569-70 (Fed. Cir. 1983); Restatement (Second) of Judgments § 29.

B. Whether Steam Drive Injection and Cyclic Steam Injection Techniques Are "Currently Used Enhanced Recovery Methods" Pursuant to the Definition of a Tar Sand

To understand the significance of the Defendant's somewhat complex argument in favor of applying issue preclusion, it is necessary, first, to explain the parties' substantive arguments regarding whether steam drive injection and cyclic steam injection are "currently used enhanced recovery techniques."

Essentially, Defendant argues: (1) "taxable" crude oil and oil from tar sands are mutually exclusive; (2) taxable crude oil includes oil produced by steam drive injection and cyclic steam injection techniques; and (3) therefore, the Plaintiffs did not produce oil from tar sands from the 8 reservoirs in question because they used steam drive injection and cyclic steam injection techniques, and they cannot prove that they did not combine them with another production method that was not used in the petroleum industry before April 2, 1980. Furthermore, Defendant argues that since steam drive injection and cyclic steam injection techniques were recognized in the June 1979 energy regulations[4] as "tertiary recovery methods" or "tertiary enhanced recovery methods," they must be "currently used enhanced recovery techniques."[5]

Defendant's argument that taxable crude oil and oil from tar sands are mutually exclusive is based on the purposes of COWPTA. The purpose of Title I of COWPTA, enacted in 1980, was to impose an excise tax on revenue produced from sales of crude oil in order to recapture "windfall profits" received by domestic oil producers that would result from the Carter Administration's decision in 1979 to phase out price controls ("Mandatory Petroleum Allocation and Price

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[4] 10 C.F.R. § 212.78 (1979).

[5] The parties do not dispute that "tertiary recovery methods," "tertiary enhanced recovery methods," and "enhanced recovery techniques" are the same. It is the understanding of the Court that "enhanced" or "tertiary" recovery methods are those techniques used to recover heavy crude oil by reducing the viscosity of the oil through raising its temperature by the application of heat, steam or other substances.

Regulations") on crude oil.[6] The purpose of Title II, which contained § 29 "Credit for Producing Fuel From A Nonconventional Source," was to encourage the reduction of dependence on foreign oil by subsidizing the development of "crude oil substitutes." *Texaco, Inc. v. Commissioner*, 101 T.C. 571, 577 (1993). *See* S. Rep. No. 96-394 at 56, *reprinted in* 1980 U.S.C.C.N. 642, 647 ("The term 'crude oil' . . . applies only to natural crude petroleum and does not include synthetic petroleum such as oil from shale or tar sands."); H.R. Conf. Rep. No. 96-817, at 114 (1980), *reprinted in* U.S.C.C.A.N. 642, 667 ("The term 'crude oil' . . . does not apply to synthetic petroleum such as oil production from shale or tar sands."). The Defendant argues that because "oil from tar sands" were "crude oil substitutes" not subject to price controls, such are not "crude oil" for the purposes of COWPTA under both Title I and Title II since profits derived from "crude oil substitutes," such as oil produced from tar sands, were not profits that the windfall profits tax ("WPT") was designed to recapture. Thus, taxable crude oil and fuel from nonconventional sources (for example, oil produced from tar sands) are mutually exclusive. Since taxable crude oil is defined to include oil produced using steam drive injection and cyclic steam injection, such oil cannot be oil from tar sands and must instead be crude oil.[7]

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[6] The price controls on crude oil were enacted pursuant to section 4(a) of the Emergency Petroleum Allocation Act (EPAA), Pub. L. No. 93-159, 87 Stat. 627 (173) (codified as amended at 15 U.S.C. §§ 751-760h) (expired 1981).

[7] *Shell I*'s analysis of COWPTA described above, for which the Defendant seek preclusive effect, mirrors the analysis in *Texaco,*

Defendant notes that, according to COWPTA, if an oil recovery project used cyclic steam injection or steam drive injection techniques, the oil produced is a category of taxable crude oil known as "Tier 3 Oil." Tier 3 Oil includes "incremental tertiary oil." § 4991(a)(C). "Incremental tertiary oil" is defined (with qualifications not relevant here) as the difference between the amount of oil removed from a reservoir in a month using a "qualified tertiary project" and

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Inc. v. Commissioner, 101 T.C. 571 (1993), the only other known case that interprets the section 29 tax credit for oil from tar sands. Texaco, like the Plaintiffs, sought a section 44D (later designated under section 29) tax credit for hydrocarbons that it claimed to be "tar sand oil." Texaco's hydrocarbons were highly viscous and "could not be economically produced through a well using only primary recovery methods." *Texaco*, 101 T.C. at 575-76. However, the Tax Court rejected Texaco's arguments and instead held that oil that could be produced using tertiary recovery methods could not be tar sand oil. at 579-80. The Tax Court determined that, following the structure of COWPTA, Title I of COWPTA determined that any hydrocarbons produced using a tertiary production method available in 1980 were crude oil subject to the WPT. At the same time, in Title I, Congress, as reflected in the legislative history of COWPTA, maintained that crude oil did not include synthetic petroleum and insofar as oil production from tar sands was a crude oil substitute, oil produced from tar sands was not crude oil. at 579. While the reference to the definition of a tar sand in defining crude oil for the purposes of Title I was not held to be necessarily determinative of the definition of a tar sand for Title II, it held that Congress would not have defined tar sands in such different ways without expressing an intent to do so. *Id.* Thus, any hydrocarbons produced by tertiary recovery methods could not considered to be tar sand oil for the purpose of section 44D.

the average monthly oil production from that reservoir prior to the passage of COWPTA § 4993(a)-(b). A "qualified tertiary recovery project" is one that, among other requirements not relevant here, uses one or more "tertiary recovery methods." § 4993(c)(2)(A). A "tertiary recovery method" refers to "any method which is described in subparagraphs (1) through (9) of section 212.78(c) of the June 1979 energy regulations." 26 U.S.C. § 4993(d)(1)(A). Section 212.78(c) of the June 1979 energy regulations, relevant to the reservoirs in this proceeding, contains "steam drive injection" and "cyclic steam injection" as methods for "a project for the enhanced recovery of crude oil" or a "qualified tertiary enhanced recovery project." 10 C.F.R. 212.78(c)(2) & (6) (1980). Thus, oil produced using one of these "tertiary recovery methods" or "tertiary enhanced recovery methods" for a "qualified tertiary (enhanced) recovery project" under the June 1979 regulations, according to the Defendant, can only be "taxable crude oil" under Title I of COWPTA. Furthermore, because the tertiary enhanced recovery methods such as steam drive injection and cyclic steam injection as listed in the June 1979 energy regulations were manifestly in use before April 2, 1980, any use of such production methods that were not combined with another enhanced recovery method not available in 1980 could not possibly be a tar sand under the FEA Ruling.

The Defendant notes further that Congress's intent in COWPTA -- to distinguish crude oil subject to the WPT tax from crude oil substitutes such as oil from tar sands not subject to the WPT and eligible for the section 29 tax credit for nonconventional fuels -- is further confirmed by the intent of the FEA Ruling to distinguish "crude oil" that was subject to the Mandatory Petroleum Allocation and Price Regulations

from "crude oil substitutes" or "synthetic products."[8] In that ruling, the FEA stated that the directs the President to promulgate price controls for "crude oil," and it was an open question as to whether Congress intended that the EPAA applied to "crude oil substitutes derived from . . . tar sands or other natural deposits that must be mined before the hydrocarbons can be extracted." 41 Fed. Reg. at 25886. After defining tar sands, the FEA determined that "Congress did not intend these products [oil produced from tar sands] to be regulated under the EPAA." *Id.* Therefore, oil produced from tar sands cannot be crude oil. Consequently, so the Defendant argues, any geologic formation from which oil is extracted by means of enhanced recovery techniques that were available in 1980, such as cyclic steam and stream drive injection, cannot satisfy the definition of a "tar sand" (unless combined with

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[8] The FEA Ruling stated in relevant part:

> At the time of the enactment of the EPAA, domestic production of crude oil substitutes derived from oil shale, coal and tar sands was, as it is now, undertaken only for experimental purposes, and the synthetic products obtained thereby are not commercially available for use as refinery or petrochemical feedstocks and were not expected to become commercially available for several years. From these facts, the FEA has concluded that the Congress clearly did not intend these products to be subject to the temporary regulation required under section 4(a) of the EPAA when it enacted the EPAA to deal with the supply shortages and dislocations in the petroleum industry that occurred late in 1973 or threatened to occur before the end of February 1975.

41 Fed. Reg. at 25886.

another enhanced recovery method not available in 1980) and any oil extracted by such enhanced recovery techniques must be crude oil.

In contrast, the Plaintiffs argue that the FEA Ruling is satisfied, thereby making any recovery of "oil produced from tar sands" subject to the section 29 tax credit if: (a) the rocks from which the oil are to be extracted contain a highly viscous hydrocarbon and (b) a portion of that hydrocarbon cannot be recovered at all or that hydrocarbon cannot be produced without changing its natural state. (Pls.' May 3, 2001, Resp. at 2.) The term "natural state," according to the Plaintiffs, refers to the "physical properties" of the extremely viscous hydrocarbons as they existed in the ground before drilling. (Pls.' Mot. for Partial Summ. J. at 17.) Theoretically then, under the Plaintiffs' interpretation of the FEA Ruling, oil recovered from a reservoir using an enhanced recovery technique which changes the physical properties of highly viscous hydrocarbons by raising the temperature of the hydrocarbons, such as steam drive injection or cyclic steam injection, but does so in conjunction with an incremental change in technology not commercially available in 1980, would satisfy the FEA definition of a tar sand and therefore be eligible for the section 29 tax credit for oil produced from tar sands.[9]

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[9] In contrast, the Defendant argues that the words "natural state" in the FEA Ruling means changing the chemical composition of the hydrocarbons extracted, such as cracking a complex hydrocarbon molecule into a simple molecule. The basis for the Defendant's interpretation of "natural state" is Treas. Reg. § 1.48-9(c)(5)(ii) (26 C.F.R.) which defines a "synthetic fuel" as a fuel that "must differ significantly in chemical composition, as opposed to physical

The application of issue preclusion, as the Defendant seeks, would make it extremely difficult for the Plaintiffs to prove that their oil was an oil produced from a tar sand unless they could prove that they used enhanced recovery techniques not available in 1980. However, the Plaintiffs claim that they recovered oil from extremely viscous hydrocarbons not recoverable in their natural state by means of "enhanced recovery technologies" that were not available in 1980. In conjunction with cyclic steam and steam drive injection, the Plaintiffs claim that they used the following methods characterized as "enhanced recovery technology" or "new technology." The "new technology" or "enhanced recovery technology advanced by the Plaintiffs include: "advanced modeling tools to design, monitor, and optimize the process, sophisticated surveillance procedures to maintain the process, advanced drilling and well completion techniques to control steam injection and maintain production, and advanced facilities designs to increase efficiency while lowering costs." (Def.'s Proposed Finding of Fact ("DPF") at 12.))

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composition, from the alternate substance used to produce it." Accordingly, an IRS General Counsel memorandum and an IRS ruling both held that, in order to become a "qualified fuel" under section 29, the fuel's production process must involve a significant chemical change. *See* G.C.M. 39548 (I.R.S.) (Nov. 30, 1984); Rev. Rul. 86-100, 1986-2 C.B. 3. There is no dispute that cyclic steam injection and steam drive recovery techniques, either in 1980 or in the form that the Plaintiffs now present before the Court, extract oil by means of pressure and application of heat and do not cause any independent change in the molecular structure of the hydrocarbon in the process.

The "advanced modeling tools to design, monitor, and optimize the thermal process" include two major components. The first component consists of "numerical thermal simulators which are "mathematical models (computer software) sophisticated enough to predict the behavior of a reservoir under various conditions." (Pls.' Statement of Genuine Issues ("PSGI") at 3.)) The Plaintiffs allege that it was not until after 1980 when these simulators became sufficiently reliable to be useful in the field. *Id.* The second component consists of a mathematical formula known as the "Vogel model," apparently developed in the 1980s, which determined the best steam injection rate for a steam flood property. *Id.* at 4.

What the Plaintiffs describe as "sophisticated surveillance tools" is in fact a fancy term for desktop computers and the sophisticated database software that was used on the computers that developed in the 1980s, logging tools and techniques, as well as inter-disciplinary team-based management of oil well projects. *Id.* at 6-7. All of these technologies, according to the Plaintiffs, were not available in 1980. The Plaintiffs' "advanced drilling and well completion projects" are terms for methods of preparing oil wells for production or injection. *Id.* at 8. These techniques were, according to the Plaintiffs, significantly improved and changed after 1980. These techniques included improved steam injector completion techniques, improved casing designs, sand control, and improved drilling techniques. *Id.* at 8-9. "Advanced facilities design" includes facilities at a reservoir that are ancillary to the oil wells themselves. These include such things as automated controls, energy cost reduction techniques, steam distribution equipment, well test equipment, production flow lines, dehydration facilities, and water treatment facilities. *Id.* at 10. The Plaintiffs claim that

they made improvements to these facilities with technology that was not available in 1980. These improvements included the use of computers, an energy efficiency study to reduce costs, a new natural gas turbine to drive an electric generator to make steam, and a device which the Plaintiffs invented and patented for distributing steam uniformly among reservoir injectors. *Id.* at 10. All of these improvements, so the Plaintiffs argue, were "enhanced recovery technology" not available in 1980.

C. The Issue of Whether Hydrocarbons Produced By Means of Enhanced Recovery Techniques In Use Prior to April 2, 1980, Are "Crude Oil" and Not "Oil Produced from Tar Sands" for the Purpose of the Section 29 Tax Credit Was Raised and Litigated in *Shell I*.

In *Shell I*, the Third Circuit, as in this case, was presented with the issue of what is the proper definition of "tar sands." In that case, the Third Circuit held that the meaning of "oil produced from tar sands" had to be divined from the statutory language and legislative history of COWPTA. After interpreting and analyzing the statutory language and legislative history of COWPTA, the Third Circuit held that the definition of "tar sands" in the FEA Ruling was "the one most compatible with congressional intent," *Shell I*, 182 F.3d at 221, because, put concisely, hydrocarbons that are produced by means of conventional oil well production methods including currently used enhanced recovery techniques in use prior to April 2, 1980, are "crude oil" and not "oil produced from tar sands" for the purpose of the section 29 tax credit. *Id.* at 223-24. This conclusion is readily apparent when the analytical steps used by the Third Circuit

in interpreting the statutory language and legislative history of COWPTA are examined closely.

The Third Circuit's rationale for finding that oil extracted by means of currently used enhanced recovery techniques in use prior to 1980 are crude oil and not oil produced from tar sands mirrors the Defendant's argument that the oil produced by steam drive injection and cyclic steam injection, both enhanced (tertiary) recovery methods, from the reservoirs at issue in the present case must be crude oil and not oil produced from tar sands for the purpose of the section 29 tax credit. First, the Third Circuit noted that in the legislative history of Title I of COWPTA, Congress explicitly distinguished "crude oil" from "oil produced from tar sands," the latter being understood as a "synthetic petroleum." *Shell I*, 182 F.3d at 222, *aff'g* 996 F. Supp. at 370 (both citing S. Rep. No. 96-394, at 56- (1979), *reprinted in* 1980 U.S.C.C.A.N. at 465. Second, the Third Circuit determined that, in enacting COWPTA, Congress intended to provide an incentive for the development of new technologies that would encourage the development and production of alternative energy sources. *Shell I*, 182 F.3d at 224, *aff'g* 996 F. Supp. at 367 (quoting from S. Rep. No. 96-394 at 6 and 87, *reprinted in* 1980 U.S.C.C.A.N. at 417 and 496). Third, the Third Circuit determined that Congress did not intend that the same hydrocarbons could be classified as both "crude oil" under Title I of COWPTA and as "oil produced from tar sands" under Title II for the purpose of the section 29 tax credit. *Shell I*, 182 F.3d at 223, *aff'g* 996 F. Supp. at 370-71. Finally, the Third Circuit determined that the FEA Ruling comports with the intent of Congress to encourage the development of new technologies by limiting the section 29 credit to crude oil substitutes that could not be obtained by

conventional methods of production, including currently used enhanced recovery techniques. *Shell I*, 182 F.3d at 224, *aff'g* 996 F. Supp. at 367.

All of the above issues raised in *Shell I* are issues that are present in this case. First, as argued in *Shell I*, the Defendant maintains that the legislative history of COWPTA establishes that Congress considered "oil produced from tar sands" to be a synthetic fuel and not "crude oil." (Def.'s Reply at 5.) Second, as in *Shell I*, the Defendant here argues that the legislative history of COWPTA shows that Congress enacted the section 29 tax credit to increase alternative energy sources that involved fuels that were not being produced when Congress enacted COWPTA. (Def.'s Mot. at 8-9.) Third, the Defendant maintains, as it did in *Shell I*, that Congress intended that the same hydrocarbons classified as "crude oil" under Title I of COWPTA cannot also be classified as "oil produced from tar sands" under section 29. *Id.* Finally, the Defendant argues here, as it did in *Shell I*, that the FEA Ruling effectuates the intent of Congress to encourage the development of new technologies and to limit the section 29 credit to "crude oil substitutes" that could not be obtained using conventional oil recovery methods, including enhanced recovery techniques. (Def.'s Reply at 14.)

Therefore, so the Defendants argue, *Shell I* decided that oil produced by means of enhanced recovery techniques that were in use prior to enactment of COWPTA, April 2, 1980, must be crude oil and not oil produced from tar sands, which is identical to an issue in the present case.

However, the Plaintiffs argue that the only issue decided in *Shell I* was that the FEA Ruling was the proper definition

of a tar sand as opposed to the alternative definition of tar sand oil they provided, namely, the supposed definition used in the petroleum industry that tar sand oil consisted of hydrocarbons which have a viscosity greater than 10,000 centipoise, measured at original reservoir temperature. *Shell I* 182 F.3d at 218. However, the extent of the Third Circuit's holding is much greater than the Plaintiffs concede. It is clear as outlined above, that the Third Circuit held that the FEA Ruling was the correct definition of a "tar sand" precisely because it held that "crude oil" and "tar sand oil" under COWPTA are not the same thing. *Id.* at 223. ("The logic and structure of the act also demonstrate that crude oil is not tar sand oil."). Similarly, the Third Circuit accepted the FEA Ruling as the correct definition of a tar sand, precisely because it held that oil produced through enhanced recovery techniques could not be tar sand oil and that any other holding would be contrary to both the statutory structure of COWPTA and the congressional intent of COWPTA as found in legislative history. "Shell's proposed definition, unlike DOE's, would classify oil producible through enhanced recovery techniques as tar sand oil. Because this classification would be contrary to the statutory scheme and to congressional intent, the District Court properly adopted the definition from DOE Ruling 1976-4." *Id.* at 223-24. This holding by the Third Circuit is particularly significant insofar as it means that if the Plaintiffs produced oil using currently used enhanced (tertiary) recovery techniques available in 1980, their oil cannot possibly be tar sand oil for the purpose of the tax credit. All of these issues were decided by the Third Circuit as essential rationales for holding that the FEA Ruling was the proper definition of tar sands.

In another bid to stave off the application of issue preclusion, the Plaintiffs argue that in *Shell I* they conceded that they were jurisdictionally precluded from arguing that their hydrocarbons would qualify as tar sand under the FEA Ruling because they failed to raise the issue in their claim for a refund. (Pls.' Opp'n at 8 n.3.) Because it could not argue at that time that its hydrocarbons would satisfy the definition of the FEA Ruling, it should have the opportunity to do so now by arguing that its hydrocarbons meet the "literal" definition of the FEA Ruling. It is difficult, however, to see how their supposed concession is at all relevant to this case. The Plaintiffs were, according the Third Circuit, only precluded from arguing that their hydrocarbons satisfied the FEA Ruling because they could not contest that their oil in *Shell I* was anything other than "tertiary oil." *Shell I*, 182 F.3d at 223 ("Because Shell does not contest the District Court's finding that its Potter Sands oil is tertiary oil, Shell's oil cannot be tar sand oil eligible for the tax credit.") Tertiary oil cannot possibly satisfy the requirement of FEA Ruling 1976-4 that the hydrocarbons cannot be extracted by "currently used enhanced recovery techniques." Tertiary recovery methods, which are used to produce tertiary oil, were manifestly in use before 1980. Jurisdictionally, therefore, the Plaintiffs were entitled to make arguments before the Third Circuit against the adoption of the FEA Ruling. It is from these arguments that the Court finds that the Plaintiffs raised and litigated identical issues in *Shell I* that are present in this case. For example, the Plaintiffs argued in their appellate brief that crude oil for the purposes of Title I of COWPTA could

likewise be tar sand oil under Title II of COWTPA.[10] Likewise, the Plaintiffs argued on appeal that the district court's reliance on legislative history for concluding that crude oil in Title I of COWPTA should apply only to natural crude oil, but not to synthetic petroleum, was erroneous.[11]

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[10] Finally, the district court said that, if the oil at issue could be both "crude oil" for purposes of Title I and "oil produced from . . . tar sands" for purposes of Title II, "the same oil would be subject to both a tax and a credit . . . . Absent some evidence that Congress intended such an anomalous result . . . the Court cannot adopt such a position . . . ."

> But this result is not at all anomalous.

Def.'s Reply to Pls.' Resp. and Obj. to Def.'s Mot. to Strike Portions of Two Affs. (*hereinafter* "Def.'s Reply Mot. to Strike") at App. 68.

[11] In its appellant brief before the Third Circuit, the Plaintiffs made the following argument:

> First, the court relied . . . on the Senate Report's statement that the term "crude oil" in Title I should apply "only to natural crude petroleum and does not include synthetic petroleum, such as oil from shale or tar sands . . . . Consequently, according to the district court, when Congress used the words "oil produced from . . . tar sands" in Title II, it must have had in mind only synthetic petroleum . . . . Any other reading, the court believed, "would result in two different definitions of tar sands under Title I and Title II."
>
> But Title I nowhere mentions, let alone defines, the words "tar sands." Nor does the Senate Report contain anything

Similarly, the Plaintiffs were not precluded from arguing before the Third Circuit, as they in fact did in their appellant's brief, that denying the section 29 tax credit to oil producible with tertiary recovery methods was tantamount to the imposition of a "new technology" requirement not found in the statutory language of COWPTA. (Def.'s Reply Mot. to Strike at App. 62-63, 65.) The Third Circuit, however, rejected the Plaintiffs' argument. *Shell I*, 182 F.3d at 224. These very points were argued by the Plaintiffs before the Third Circuit for the specific purpose of opposing the district court's holding that the FEA Ruling was the correct definition of a tar sand.

Furthermore, the Third Circuit opinion in *Shell I* itself clearly evidences that the Plaintiffs argued in the prior proceeding that oil produced using enhanced (tertiary) recovery methods could be classified as tar sand oil as well as crude oil. *Shell I*, 182 F.3d at 221-22 ("But Shell contends that tertiary oil can be classified as both crude oil and tar sand oil, arguing that its Potter Sands oil, extracted through enhanced (tertiary) recovery methods, is also tar sand oil eligible for the Title II tax credit."). *See also* Def.'s Reply Mot. to Strike at App. 63. However, the Third Circuit rejected the Plaintiffs' argument, stating instead, "we agree

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> resembling a definition. One cannot fairly read the words "synthetic petroleum, such as oil from shale or tar sands" to indicate that only synthetic petroleum could qualify as oil from tar sands. An equally plausible understanding is that "oil from shale or tar sands" was merely an example of oil that could be processed into "synthetic petroleum."

Def.'s Reply Mot. to Strike at App. 66.

with the District Court that oil produced with tertiary extraction methods available in 1980, such as steam injection, does not qualify for the non-conventional source credit." *Id.* at 224.

Finally, the Plaintiffs maintain that issue preclusion is inappropriate in this tax refund case because, pointing to an exception to the doctrine of issue preclusion in tax cases, the facts in the previous case must be identical to those in the second case and the legal issue in both cases must be inseparable. *Commissioner v. Sunnen*, 333 U.S. 591, 601, 92 L. Ed. 898, 68 S. Ct. 715, 721 (1948).[12] The Plaintiffs cite the following relevant part of *Sunnen*: "before a party can invoke the collateral estoppel doctrine in these circumstances, the legal matter raised in the second proceeding must involve the same set of events or documents and the same bundle of legal principles that contributed to the rendering of the first judgment." *Id.* at 602. Because there are more reservoirs at issue in *Shell I* than in this case, so the Plaintiffs argue, the facts in *Shell I* cannot be identical to the present case; and therefore collateral estoppel cannot be applied.

However, the Plaintiffs fail to mention in their briefs the case of *Montana v. United States*, 440 U.S. 147, 161, 59 L.

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[12] The Plaintiffs also cite *Bilzerian v. United States*, 41 Fed. Cl. 134, 138 (1998) for the same proposition, though the Court does not see how that case has any relevance to the *Sunnen* rule at all. *Bilzerian* teaches that a criminal conviction for conspiracy to defraud the IRS and the SEC for failure to appropriate forms is not an identical issue, for the purposes of issue preclusion, to the legality and, therefore, the deductibility of a payment under § 162(c)(2).

Ed. 2d 210, 99 S. Ct. 970 (1979), which distinguishes *Sunnen* insofar as the *Sunnen* rule only applies to those situations where a "change in controlling legal principles had occurred between [the prior suit] and the instant suit." *Id. See also Bingaman v. United States*, 127 F.3d 1431, 1437 (Fed. Cir. 1997); *Arkla, Inc. v. United States*, 37 F.3d 621, 625 n.4 (Fed. Cir. 1994); Thus, if there is not "a significant change in the legal climate," *Montana*, 440 U.S. at 161 (*quoting Sunnen*, 333 U.S. at 606) between the prior suit and the instant suit, issue preclusion is warranted.[13]

In the present case the Plaintiffs have not pointed to (nor has the Court found) any change in the controlling legal principles of the section 29 tax credit between the tax years at issue in *Shell I* and the tax years at issue in the present case. Moreover, while it is true that there are more reservoirs at issue in the present case than in *Shell I*, the outcome of the legal issue for which the Defendant seeks preclusive effect -- namely, that hydrocarbons produced by enhanced recovery methods available in 1980 are crude oil for the purposes of the section 29 tax credit and cannot be oil produced from tar sands -- does not depend on which reservoirs are at issue in any particular case. Oil recovered by means of pre-1980 enhanced recovery methods either qualify as oil produced from tar sands under section 29 or they do not so qualify, no matter which reservoirs are at issue and no matter which tax year is at issue.

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[13] A change in controlling legal principles that renders the application of issue preclusion inappropriate would be when "there has been some marked advance or alteration in relevant orientation, approach, reasoning, or principles." *CBN Corp. v. United States*, 176 Ct. Cl. 861, 865, 364 F.2d 393 (1966).

Therefore, this Court holds that the issue of whether hydrocarbons that are produced by means of enhanced recovery techniques in use prior to April 2, 1980, are "crude oil" and not "oil produced from tar sands," for the purpose of the section 29 tax credit, was raised and litigated in *Shell I*.[14]

D. The Third Circuit's holding that hydrocarbons produced by enhanced recovery techniques in use prior to April 2, 1980, are, for the purpose of the section 29 tax credit, "crude oil" and not "oil produced from tar sands" was necessary to the judgment.

If a matter of law or fact has been decided by a court and is necessary to its judgment, then that "decision is conclusive in a subsequent suit based on a different cause of action involving a party to the prior litigation." *United States v. Mendoza*, 464 U.S. 154, 158, 78 L. Ed. 2d 379, 104 S. Ct. 568 (1984). However, the issue in question need not be so

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[14] Although *Shell I* did not explicitly interpret the words "natural state" in the definition of a tar sand in the FEA Ruling, if steam drive and cyclic steam are "currently used enhanced recovery techniques" as held by *Shell I*, then by necessary implication "natural state" cannot mean a change in the physical property of the hydrocarbons, as the Plaintiffs maintain, because these enhanced recovery techniques recover oil by changing the physical property of the hydrocarbon, i.e., raising the temperature and pressure of the rocks from which the oil is extracted. Concurrently, the Defendant's proffered definition of "natural state" as a change in chemical composition is consistent with Shell I's holding that oil produced from a tar sand was contemplated by Congress, both in COWPTA and the EPAA, to be a "crude oil substitute."

crucial to the judgment that the judgment could not stand without it; instead, the purpose of this requirement is to prevent the adjudication of collateral issues in a prior proceeding from precluding reconsideration in a later proceeding. *Mother's Restaurant*, 723 F.2d at 1571, *Restatement (Second) of Judgments* § 27, cmt. h (1980).

The Plaintiffs argue that the Third Circuit's interpretation of the FEA Ruling is dicta because the only question before the Third Circuit was which of the two competing definitions of a tar sand applied to the section 29 tax credit, namely, whether the FEA Ruling or the industry standard was the correct definition. (Pls.' Resp. at 9.) Thus, the Third Circuit's holding that hydrocarbons produced by means of enhanced (tertiary) recovery techniques in use prior to April 2, 1980, cannot be an oil produced from a tar sand consists of only, according to the Plaintiffs, "generalized discussions about technologies not necessary to the application of the words of FEA 1976-4." (Pls.' Resp. at 10.)

However, this Court cannot accept the Plaintiffs' sweeping view of the nature of dicta. Dicta are "words of an opinion entirely unnecessary for the decision of the case." *King v. Erickson*, 89 F.3d 1575, 1582 (Fed. Cir. 1996, *rev'd on other grounds*, 522 U.S. 262 (1998), *quoting Black's Law Dictionary* 1072 (6th Ed. 1990). Those portions of an opinion necessary to the result are binding. *Seminole Tribe of Florida v. Florida*, 517 U.S. 44, 66-67, 134 L. Ed. 2d 252, 116 S. Ct. 1114 (1994). The Third Circuit came to the conclusion, affirming the district court, that the FEA Ruling was the correct definition of an oil produced from tar sands precisely because that definition was most congruous with congressional intent; namely, that Congress intended that tar

sand oil was not crude oil, but instead was a crude oil substitute and that any hydrocarbons extracted with currently used enhanced oil recovery methods were, for the purposes of COWPTA, crude oil and not tar sand oil. *Shell I*, 182 F.3d at 221-22. These findings are hardly generalized discussions about technologies not essential to the holding or somehow unnecessary to the decision of the case; instead these findings are at the very heart of the reasoning of the Third Circuit's adoption of the FEA Ruling as the correct definition of "oil produced from tar sands."

Therefore, the Court finds that the Third Circuit's holding that hydrocarbons which are produced by means of currently used enhanced recovery techniques in use prior to April 2, 1980, are "crude oil" and not "oil produced from tar sands" for the purpose of the section 29 tax credit was necessary to the judgment.

E. The Third Circuit's holding that hydrocarbons which are produced by means of enhanced recovery techniques in use prior to April 2, 1980, are "crude oil" and not "oil produced from tar sands" for the purpose of the section 29 tax credit was fully and fairly litigated.

There can be no dispute that the Plaintiffs had a full and fair opportunity to litigate this issue in *Shell I*. The Plaintiffs were fully represented by counsel during the course of *Shell I*. *Shell I*, 182 F.3d at 214. Furthermore, the Plaintiffs did not suffer any procedural disadvantages because the Plaintiffs did in fact avail themselves of the opportunity to dispute whether hydrocarbons produced by enhanced recovery techniques in

use prior to April 2, 1980, are crude oil and not oil produced from tar sands for the purposes of the section 29 tax credit.

Consequently, the Court holds that the Plaintiffs are estopped from relitigating the issue of whether hydrocarbons produced by enhanced recovery techniques in use prior to April 2, 1980, are crude oil and not oil produced from tar sands for the purposes of the section 29 tax credit. Thus, the Court holds that hydrocarbons produced from the reservoirs at issue using enhanced recovery techniques in use prior to April 2, 1980, are crude oil under Title I of COWPTA and not oil produced from tar sands. Having accepted the FEA Ruling as the proper definition of a tar sand; and having accepted that hydrocarbons produced by "currently used enhanced recovery methods" in use prior to 1980, including steam drive injection and cyclic steam techniques, as such do not satisfy the FEA Ruling's definition of a tar sand but instead are crude oil under Title I of COWPTA; and, finally, having accepted the reasoning of *Shell I* that hydrocarbons which satisfy the definition of "crude oil" under Title I of COWPTA cannot satisfy the FEA Ruling either, the Court now turns to the issue of whether there is an absence of evidence that the Plaintiffs produced anything other than crude oil, and whether there is an absence of evidence that Plaintiffs produced oil from tar sands. To do so, the Court must determine whether incremental changes in technology ("new technology") or "enhanced recovery technology" used by the Plaintiffs, as described in § II(B) *supra*, in conjunction with enhanced recovery methods already in commercial use prior to 1980 can be considered to be a currently used enhanced recovery technique. These issues will be discussed in more detail in the following sections.

III.Standard for Summary Judgment

Summary judgment is appropriate when there are no genuine issues of material fact and the moving party is entitled to judgment as a matter of law. RCFC 56(c); *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 247, 106 S. Ct. 2505, 2509-10, 91 L. Ed. 2d 202 (1986); *Jay v. Secretary, DHHS*, 998 F.2d 979 (Fed. Cir. 1993). The party moving for summary judgment bears the initial burden of demonstrating the absence of any genuine issues of material fact. *Celotex Corp. v. Catrett*, 477 U.S. 317, 325, 91 L. Ed. 2d 265, 106 S. Ct. 2548 (1986). However, this burden may be discharged if the moving party demonstrates that there is an absence of evidence to support the non-moving party's case. *Id.* ("The burden on the moving party may be discharged by 'showing' -- that is, point out to the district court -- that there is an absence of evidence to support the non-moving party's case.") If the moving party makes such a showing, the burden then shifts to the non-moving party to demonstrate that a genuine factual dispute exists. *Id.* at 322. In order for a factual dispute to be genuine, the evidence must be such that a reasonable jury or trier of fact could return a verdict for the non-moving party. *Anderson*, 477 U.S. at 248 (1986). In order for the non-moving party to demonstrate that a genuine factual dispute exists, by means of an opinion, it must produce a factual foundation in sufficient detail in order for the Court to determine whether the opinion would support a verdict for the non-moving party, with all reasonable inferences drawn in favor of the non-movant. *Arthur A. Collins, Inc. v. Northern Telecom, Ltd.*, 216 F.3d 1042, 1047-48 (Fed. Cir. 2000).

IV. The Plaintiffs Do Not Have Sufficient Evidence To Show That The Hydrocarbons They Produced Are Oil From Tar Sands And Not Crude Oil.

The Defendant maintains that the Plaintiffs cannot prove certain essential elements of their claim that the hydrocarbons they produced from the 8 reservoirs at issue during the years 1988 and 1989 are oil from tar sands, as defined by the FEA Ruling. First, it argues that the Plaintiffs cannot show that the hydrocarbons they produced were not taxable crude oil within the definition of Title I of COWPTA.[15] This is so because the Plaintiffs used cyclic steam injection and/or stream drive injection oil-well production methods in commercial use before 1980 in 7 out of the 8 fields at issue.[16] Those production methods, according to the Defendant, are tertiary recovery methods, and oil extracted by means of such tertiary recovery methods is crude oil subject to the windfall profits tax and cannot be oil from tar sands. Second, the Defendant

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[15] The 8 reservoirs at issue are: (1) Coalinga Etchegoin; (2) Kern River Series; (3) North Midway Sunset - Potter Sands; (4) Yorba Linda Upper Conglomerate; (5) McKittrick Tulare; (6) Cat Canyon Basal - Sisquoc; (7) East Cat Canyon - Brooks; and (8) Casmalia - Monterrey. The Plaintiffs allege that during 1988 and 1989, Shell Western E&P ("SWEPI"), a Shell Petroleum affiliate, produced oil from tar sands by means of wells drilled after December 31, 1979, and before January 1, 1993, from the 8 reservoirs at issue.

[16] The Plaintiffs have not revealed the production process at the Casmalia reservoir. Because the Plaintiffs have not made any attempt to show that they are entitled to the section 29 credit with respect to this reservoir, summary judgment is granted in favor of the Defendant with respect to the Casmalia reservoir.

maintains that the Plaintiffs cannot show they used any production method other than "conventional oil well production methods including currently used enhanced recovery techniques," as stated in FEA Ruling 1976-4, to extract hydrocarbons from the reservoirs at issue. Both arguments mirror each other and therefore shall be considered together.

It is undisputed by the Plaintiffs that they used cyclic steam injection or steam drive injection methods in producing hydrocarbons from the reservoirs at issue. Following the Court's prior determination that such methods in use prior to 1980 produced crude oil and not oil from tar sands, in the absence of evidence that the cyclic steam and steam drive injection techniques used by the Plaintiffs were not in commercial use prior to 1980, the Plaintiffs cannot prove that what they produced was anything other than crude oil and not oil produced from tar sands. The Plaintiffs, however, maintain that they produced oil from the reservoirs at issue by means of enhanced recovery "technology" not available in 1980. First, they maintain that if they used "new technology" not available in 1980 in conjunction with cyclic steam and steam drive injection production methods to produce the hydrocarbons at issue, such oil would qualify for the section 29 credit as oil produced from tar sands. This argument is premised on the Third Circuit's statement in *Shell I* that "where the definition of an energy source is unclear, Congress's directive that the eligible energy sources to be subsidized 'typically involve new technologies' assists us in interpreting the provision." *Shell I*, 182 F.3d at 225. This is confirmed, in the eyes of the Plaintiffs, by the section 29(b)(5) offset provision which provides that a section 29 credit for producing oil from tar sand must be reduced by any

credit allowed under section 43 with respect to the same project. *See Shell Petroleum, Inc. v. United States*, 46 Fed. Cl. 719, 723-24 (2000) (describing the section 43 tax credit for using tertiary recovery methods). According to the Plaintiffs, the existence of section 29(b)(5) would be superfluous if a steam-based project could not qualify for a section 29 credit. The Plaintiffs propose that "new technology" consists of incremental advances in technology made by combining several existing technologies in ways not previously utilized to improve domestic oil production. This proposal was advanced by Dr. James R. Schlesinger, former Secretary of Energy. *See* Schlesinger Aff. PP 23, 25. The "new technology" that they claim to have used includes advanced modeling tools, sophisticated surveillance procedures, advanced drilling and well completion techniques, and advanced facilities designs.[17] (Pls.' Statement of Genuine Issues *hereinafter* "PSGI" 3 and 10.) The Plaintiffs characterize these technologies as "enhanced recovery technologies" which are not "currently used enhanced recovery techniques" for the purposes of the FEA Ruling.[18]

The Defendant concedes that a combination of steam drive or cyclic steam injection techniques with another technology which is necessary for production of hydrocarbons from the

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[17] These technologies are briefly described in § II(b), *supra*.

[18] The Court rejects the Plaintiffs' argument that the Government is not entitled to summary judgment without establishing that the Plaintiffs did not use new technology. Under *Celotex*, it is enough for the Defendant to "point out" to the Court that there is an absence of evidence that it used "new technology" to produce the oil at issue. *See Celotex*, 477 U.S. at 322-23, 325.

reservoir and not in use in 1980 would qualify as oil produced from tar sands under § 29. (Def.'s Reply at 15.) However, it distinguishes such combinations from the "new technologies" proffered by the Plaintiffs insofar as none of the technologies offered by the Plaintiffs are technologies used in production. More specifically, the Defendant argues that none of what the Plaintiffs call "enhanced recovery technology" or "new technology" produce hydrocarbons. (Def.'s Reply at 18.) The Defendant argues that a production method is a technology that "move[s] hydrocarbons in a reservoir to a well bore so they can be lifted to the surface." (Def.'s Reply at 17.) This is in contrast to the Plaintiffs' proffered definition, based on the declaration of its expert, Dr. Roger Hite, that a production process consists of "all aspects of production from those work processes that begin immediately after a property has been acquired or a reservoir discovered and end when the oil is sold for shipment to a refinery." (PSGI at 12.)

There are several insurmountable difficulties with the Plaintiffs' arguments. First, the existence of the section 29(b)(5) offset provision does not result in a superfluous interpretation of the section 29 tax credit. As the Defendant points out, the offset provision could come into operation if a taxpayer purchased a cyclic steam or steam drive injection technique in conjunction with a production technique that was new or had not been combined with cyclic steam or steam drive injection before 1980 and used the combination to produce oil from tar sands. *Shell Petroleum, Inc.*, 46 Fed. Cl. at 724 n.8. The Plaintiffs characterize their "new technology" as an "enhanced recovery *technology*" not available in 1980. This is a subtle but significant shift from the text of the FEA Ruling which excludes hydrocarbons extracted by means of "enhanced recovery *techniques*" from the definition of a tar

sand. The term "enhanced recovery technology" suggests an incremental development in pre-existing methods of production, whereas "enhanced recovery technique" connotes a method in and of itself. Accordingly, the Plaintiffs' definition of a production process is incorrect because it does not correspond with the literal text of the FEA Ruling insofar as the Plaintiffs must prove that they used an enhanced recovery *technique* not available in 1980. The Plaintiffs' proposed definition of a production process, along with their understanding of "new technology" as reflected in Dr. Schlesinger's declaration, is also too broad because it would encompass almost any ancillary task associated in some way with oil production. Almost any conceivable improvement to any ancillary technology associated in some way with pre-existing enhanced recovery methods could qualify for the section 29 tax credit. Furthermore, the Plaintiffs' definition of a "production method" is a misstatement of Dr. Hite's definition. In his declaration, Dr. Hite characterizes "a number of work processes which begin immediately after a property has been acquired (or a reservoir has been discovered) and end when the oil is sold for shipment to a refinery" as "production technology." (Pls.' Resp. at App. 0129.) Dr. Hite describes the "work process" of "production" as "to get the oil out from the reservoir to the surface." *Id.* Evidently, Dr. Hite contemplated that there are many technologies associated with production in a broad sense, but such technologies are not, strictly speaking, to be identified as the "work process" of "production." Such an understanding is consistent with the enhanced recovery techniques contained within the June 1979 energy regulations, all of which consist of production techniques in the strict sense and not with technologies associated with production in a general sense.

The Defendant's definition of a production method, therefore, is sensible and consonant with Dr. Hite's definition of the "work process" of "production."[19] None of the developments of technology that the Plaintiffs have pointed to as "new technology" or "enhanced recovery technology" are the work process of production. While all of the improvements demonstrated by the Plaintiffs, such as computers, software, testing equipment, generators, steam distributors, and manpower deployment are ancillary aides that make cyclic steam or steam drive injection production processes more efficient and cost-effective, these improvements do not actually move hydrocarbons or, in Dr. Hite's words, "get the oil out from the reservoir to the surface."

A further illustration of the difference between a genuine work process of production and the Plaintiffs' supposed "enhanced recovery technology" can be found in a private letter ruling of the IRS.[20] In P.L.R. 9113019, the IRS ruled that the use of cyclic steam, together with "the inclusion of . . . diluent and natural gas in the injection and production

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[19] Likewise, in *Shell I*, the Third Circuit held that "oil capable of extraction through any of the enhanced production methods set forth in 10 C.F.R. § 212.78(c) is not tar sand oil." *Shell I*, 182 F.3d at 222.) Thus, it is clear that an enhanced recovery method is a process which extracts hydrocarbons from the ground.

[20] Written determinations by the IRS, unless otherwise established by regulations, cannot be used or cited as precedent. 26 U.S.C. § 6110(k)(3). The Court, therefore, expresses no opinion as to whether this process in itself would in fact qualify for the section 29 tax credit.

phases under the particular conditions and circumstances here distinguishes this process from any conventional cyclic steam injection project." P.L.R. 9113019 (Dec. 28, 1990). In the injection phase, "hydrocarbon gas and a diluent hydrocarbon mixture are injected concurrently with steam . . . . The concurrent injection of gas, steam, and diluent hydrocarbons results in an injection front composed of steam, gas, diluent vapor, diluent liquid, and condensed steam. Because the entire producing zone surrounding the well is exposed to the hot fluids, these fluids penetrate the tar sand formation, and the hot gas and diluent commingle with the tar. The diluent fluidizes the tar, enabling it to flow." *Id.* Unlike the injection method described in P.L.R. 9133019, none of the supposed "new technology" or "enhanced recovery technology" not available in 1980 are injected into the well to penetrate a highly viscous hydrocarbon in order to, at least in this case, change the tar from its immobile state to a more fluid state. Instead, the function of the new technology is to assist in the more efficient use of steam-based injection methods that were commercially available in 1980.[21] Likewise, in the production

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[21] There is a seeming inconsistency between the Defendant's insistence that the term "not recoverable in its natural state" in the FEA Ruling refers to a change in the chemical composition of the highly viscous hydrocarbon and the IRS's determination in P.L.R. 9113019 that an enhanced recovery technique that changes the physical state of the hydrocarbon, not available in 1980, would qualify as an "oil produced from tar sands." The Court cannot determine whether the combination of steam, natural gas, and diluent would change the chemical composition of the extracted hydrocarbons in some way. Any inconsistency, however, is immaterial to the outcome of this decision because the Court has already held that, for purposes of issue preclusion, "natural state"

phase of the technique found in the private letter ruling, "diluent is injected throughout this [phase]." In contrast, the Plaintiffs' "new technology" or "enhanced recovery technology" not available in 1980 is not physically injected into the well or otherwise used to remove the highly viscous hydrocarbon from the well.

Accordingly, the Plaintiffs have failed to raise a genuine issue of material fact that they used production methods to extract "extremely viscous hydrocarbons" other than by means of cyclic steam or steam drive injections that were in commercial use prior to 1980, which, under Title I of COWPTA, would qualify as crude oil subject to the WPT and would not qualify as oil produced from tar sands under section 29.[22]

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refers to a change in the chemical composition of the highly viscous hydrocarbon, and also that the "enhanced recovery technologies" proffered by the Plaintiffs in this case would not, in and of themselves, change the physical state of the highly viscous hydrocarbon. In any event, private letter rulings are not normally binding precedent.

[22] The Plaintiffs argue that somehow they are being required to satisfy a definition of a tar sand other than the FEA Ruling, which they claim is tantamount to the revocation of a technical advice memorandum issued to them by the IRS holding that "FEA Ruling 1976-4 provides the proper definition of a tar sand for purposes of the credit under section 29 of the Code for production of fuels from nonconventional sources." Tech. Adv. Mem. 89400004 (June 20, 1989). Nothing in the Court's analysis, however, is contrary to the technical advice memorandum because the IRS did not address the issue of whether the Plaintiffs recovered oil by means of "currently used enhanced recovery techniques," and it explicitly held that any

Therefore, in the absence of any evidence that the hydrocarbons produced by the Plaintiffs at any of the reservoirs at issue are anything other than crude oil under Title I of COWPTA, and cannot be oil produced from tar sands, the Court holds that the Plaintiffs cannot show that they produced oil from tar sands for the purposes of the section 29 tax credit.[23]

V. Conclusion

Because the Plaintiffs cannot show that they are entitled to the section 29 tax credit, the Court GRANTS the Defendant's motion for summary judgment and DENIES the Plaintiffs'

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question of whether the Plaintiffs' production was in fact oil produced from tar sands was a factual determination under the jurisdiction of the District Director of the IRS. In applying and interpreting the FEA Ruling, this Court holds that the Plaintiffs have failed to show that they have produced hydrocarbons by means of anything other than a "currently used enhanced recovery technique." The Plaintiffs' complaint that they have been deprived of the benefit of Technical Advice Memorandum 8940004 or otherwise required to prove they produced oil from a tar sand on the basis of a definition of a tar sand other than the FEA Ruling is groundless.

[23] The Defendant also argues that there is an absence of evidence that the Plaintiffs could not have produced hydrocarbons from any of the reservoirs at issue by means of enhanced recovery methods not in commercial use in 1980, which it claims to be an essential element to the Plaintiffs' claim. However, the Court need not resolve this issue because the Plaintiffs' claims fail on other grounds.

motion for partial summary judgment.[24] The Clerk of the Court is directed to enter judgment, with prejudice, in favor of the Defendant and dismiss the complaint.

IT IS SO ORDERED.

/s/_____
EDWARD J. DAMICH, Judge

[24] The Court grants summary judgment in favor of the Defendant with respect to the Casmalia reservoir because they have not revealed the production process for that reservoir.

APPENDIX E

UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 97-7639

[Filed June 24, 1999]

SHELL PETROLEUM, INC., and Subsidiary Corporations,
Appellant

v.

UNITED STATES OF AMERICA
Appellee

On Appeal from the
United States District Court
for the District of Delaware
D.C. Civil Action No. 93-cv-00508
Honorable Joseph J. Farnan, Jr.

JUDGES: Before: SLOVITER, SCIRICA and ALITO, Circuit Judges.

OPINION

SCIRICA, Circuit Judge.

This is an appeal of the denial of a tax credit under the Crude Oil Windfall Profit Tax Act, Pub. L. 96-223, 94 Stat. 229 (1980) (codified in scattered sections of 7, 19, 26, and 42 U.S.C.) (repealed in part 1988) ("COWPTA") which grants oil producers an income tax credit of $ 3.00 for each barrel-of-oil equivalent of "oil produced from . . . tar sands" extracted through wells drilled between January 1, 1980 and December 31, 1992. The resolution of this case turns on the proper definition of "oil produced from tar sands," which the Act does not define. Shell contends the definition should be derived from commonly accepted usage in the petroleum industry and asserts that when the statute was enacted in 1980, "tar sand oil" meant "oil so viscous[1] that it cannot be recovered economically through 'primary production methods'[2]-- i.e., methods used in ordinary oil fields." The

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[1] "Viscosity is the measure of a fluid's resistance to flow. In an oil reservoir, viscosity is the measure of the oil's resistance to movement through the reservoir rock to the well-bore. Given uniform pressure and rock properties, a more viscous oil will move through the reservoir more slowly than a less viscous oil." *Shell Petroleum, Inc. v. United States*, 996 F. Supp. 361, 362 n.1 (D. Del. 1997).

[2] Crude oil is ordinarily extracted through wells from underground reservoirs, which are formations of sand or rock containing tiny pore spaces permeated with oil. There are three types of production through wells: Primary production depends on the inherent pressure in an oil reservoir. Secondary production involves the injection of

government maintains the proper definition may be found in Department of Energy Ruling 1976-4, which defines "tar sands" as "the several rock types that contain an extremely viscous hydrocarbon which is not recoverable in its natural state by conventional oil well production methods including currently used enhanced recovery techniques." Department of Energy Ruling 1976-4, 10 C.F.R. ch. II Rulings 371, 372 (1980).[3] Shell concedes that it is not entitled to a refund if we accept the DOE Ruling definition. Following a bench trial, the District Court adopted the definition of tar sands crafted by the DOE Ruling and denied the refund. *See Shell Petroleum, Inc. v. United States*, 996 F. Supp. 361, 372 (D. Del. 1997). Because we substantially agree with the District Court's well reasoned opinion, we will affirm.

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gas or water into a reservoir to increase pressure. Tertiary (or enhanced) production, such as the injection of steam into the reservoir, increases its temperature (making the oil less viscous) or alters its other characteristics. Shell's definition classifies oil recoverable only by means of secondary or enhanced/tertiary production methods as tar sand oil.

In the petroleum industry, crude oil is commonly designated as "light," "medium," or "heavy," depending on its density; heavier oils are generally more viscous. Primary production is effective with lighter, lower-viscosity oil, but more viscous oils require secondary or enhanced production methods.

[3] The Ruling was initially issued by one of DOE's predecessor agencies, the Federal Energy Agency. By the time COWPTA was enacted, the Ruling had been redesignated a DOE Ruling in the Code of Federal Regulations.

I

A

Beginning in 1973, world oil prices quadrupled in less than a year after the Organization of Petroleum Exporting Countries embargoed oil sales to Western nations and then fixed prices above market levels. *See* Gary D. Allison, Energy Sectionalism: Economic Origins and Legal Responses, 38 Sw. L.J. 703, 705 (1984). Congress responded with the 1973 Emergency Petroleum Allocation Act (EPAA), Pub. L. No. 93-159, 87 Stat. 627 (1973) (codified as amended at 15 U.S.C. §§ 751-760h) (expired 1981), authorizing the President to regulate prices and allocate supplies of crude oil and related petroleum products.

In 1976, the Federal Energy Agency, which administered EPAA, issued Ruling 1976-4 in response to "inquiries with respect to the applicability of the [EPAA price and supply controls] to the so-called synthetic fuels (or crude oil substitutes) processed from oil shale, tar sands, coal, and other natural deposits that must be mined[4] before the crude oil substitute can be extracted. " Department of Energy Ruling 1976-4, 10 C.F.R. ch. II Rulings at 371. According to FEA,

> at the time of enactment of the EPAA, domestic production of crude oil substitutes derived from oil

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[4] Tar sand oil can be produced by mining the tar sand and subsequently separating the oil from the mined rock through physical and chemical processes.

> shale, coal and tar sands was, as it is now, undertaken only for experimental purposes, and the synthetic products obtained thereby were not commercially available for use as refinery or petro-chemical feedstocks and were not expected to become commercially available for several years.

Id. at 372. Therefore, FEA concluded that synthetic fuels processed from tar sands were not subject to the EPAA regulatory scheme. *See id.* at 373.

The Emergency Petroleum Allocation Act proved counterproductive. Price controls reduced incentives to produce oil domestically and increased domestic oil consumption overall, making America more dependent on expensive imported oil. See Atlantic Richfield Co. v. United States Dep't of Energy, 655 F.2d 1118, 1121 (Temp. Emer. Ct. App. 1981). Oil prices fell in real terms after 1975, but world oil prices doubled in 1979, when the Iranian revolution severely curtailed oil exports. *See Allison*, *supra*, at 705-06. The Carter administration announced in 1979 it would phase out price controls, dramatically increasing domestic producers' short-term profits. *See* H.R. No. 96-304, at 5-7 (1979), reprinted in 1980 U.S.C.C.A.N. 587, 592-94. For this reason, Congress responded to the price decontrols with the Crude Oil Windfall Profit Tax Act. Title I ("Windfall Profit Tax on Domestic Crude Oil") imposed an excise tax on revenue from producer sales of crude oil, designed to capture the windfall profit. *See* 26 U.S.C. §§ 4986-98 (1982) (repealed 1988). To avoid suppressing the domestic oil supply, new production and other production considered sensitive to price fluctuations were taxed at lower rates or

exempted. *See id.* §§ 4987(b), 4991-93; S. Rep. No. 96-394, at 2 (1979), reprinted in 1980 U.S.C.C.A.N. 410, 414. More importantly for our purposes, Title II ("Energy Conservation and Production Incentives") sought to reduce American dependence on imported oil by various means, including a tax credit "for producing fuel from a nonconventional source. "26 U.S.C.A. § 29 (West Supp. 1999) (as amended 1981, 1983, 1984, 1986, 1988, 1990, 1992, and 1996) (originally designated § 44D).[5] Among the fuels qualified to receive the

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[5] Credit for producing fuel from a nonconventional source

(a) Allowance of credit.--There shall be allowed as a credit against the tax imposed by this chapter for the taxable year an amount equal to--

(1) $ 3, multiplied by

(2) the barrel-of-oil equivalent of qualified fuels--

(A) sold by the taxpayer to an unrelated person during the taxable year, and

(B) the production of which is attributable to the taxpayer.

. . . .

(c) Definition of qualified fuels.--For purposes of this section--

(1) In general.--The term "qualified fuels" means--

(A) Oil produced from shale and tar sands

. . . .

(f) Application of section.--This section shall apply with respect to qualified fuels--

(1) which are--

(A) produced from a well drilled after December 31, 1979, and before January 1, 1993

26 U.S.C.A. § 29.

credit was "oil produced from shale and tar sands" through wells drilled between January 1, 1980 and December 31, 1992. *Id.* §§ 29(c)(1)(A), (f)(1)(A).

B

In 1983 and 1984, the tax years in question, Shell Petroleum, Inc. and certain subsidiary corporations owned working interests in properties in the Midway Sunset Field, Kern County, California. Part of the Midway Sunset Field lies over a reservoir known as "the Potter Sand formation" or "Potter Sands." For over a decade Shell had been extracting oil from Potter Sands through two steam injection techniques (steam soak, begun in 1963, and steam flood, begun in 1971). By 1980, both were well established and widely accepted enhanced recovery techniques in the petroleum industry.[6]

In its 1983 and 1984 tax returns, Shell did not seek the nonconventional source tax credit for Potter Sands oil, but in 1991 Shell filed amended tax returns claiming credits of $5,351,150 for Potter Sands oil produced during 1983 and 1984 from wells drilled after December 31, 1979. The tax credits were denied and Shell timely filed suit. Relying in part on the "instructive" analysis of *Texaco Inc. v. Commissioner*, 101 T.C. 571 (1993),[7] the District Court, as noted, entered

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[6] The record does not disclose whether any oil was produced from Potter Sands during 1983 and 1984 other than through steam injection, but Shell does not claim to have used any technology that was not well established in 1980.

[7] Texaco argued certain high-viscosity crude oil it had produced was tar sand oil. The Tax Court accepted that when COWPTA was

judgment for the United States. See Shell, 996 F. Supp. at 371. Shell now appeals.[8]

As we will discuss, Title I of COWPTA establishes that Shell's Potter Sands oil is crude oil. But the structure of the statute and the legislative history establish that crude oil is not

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enacted "tar sand oil" was "generally understood" within the petroleum industry as oil that "could not be economically produced through a well using only primary recovery methods," *see Texaco*, 101 T.C. at 575-76, but rejected that definition for two reasons. First, Congress sought to subsidize "alternative energy sources [that] typically involve new technologies." S. Rep. No. 96-394, at 87, reprinted in 1980 U.S.C.C.A.N. at 496. Crude oil produced with technology widely available when the credit was enacted, the Texaco court reasoned, was not such an energy source. *See Texaco*, 101 T.C. at 576-77. Second, Title I defined oil produced using tertiary production methods available in 1980 as crude oil subject to the windfall profit tax. But the discussion of Title I in the legislative record indicated that Congress considered "oil produced from tar sands" to be synthetic petroleum, which Congress distinguished from crude oil. Therefore, the Tax Court concluded that oil producible using tertiary recovery methods could not be tar sand oil unless Congress had intended to give different meetings to the term "oil produced from tar sands" as used in the text of Title II and in the Title I Committee Reports, an unlikely scenario. *See id.* at 579-80.

[8] The District Court had original jurisdiction under 28 U.S.C.A. § 1346 (a)(1) (West 1993). We have appellate jurisdiction under 28 U.S.C.A. § 1291 (West 1993). Questions of statutory interpretation are reviewed de novo. *See United States v. West Indies Transport, Inc.*, 37 V.I. 579, 127 F.3d 299, 307 (3d Cir. 1997). Findings of fact made following a bench trial are reviewed for clear error. *See Cooper v. Loper*, 923 F.2d 1045, 1049 (3d Cir. 1991).

tar sand oil. Therefore, Shell's oil cannot be tar sand oil. Furthermore, the legislative history establishes that the nonconventional source tax credit was intended to foster new energy technologies, whereas Shell's Potter Sands oil was produced in 1983 and 1984 using widely available means of production.

II

"'Where . . . resolution of a question of federal law turns on a statute and the intention of Congress, we look first to the statutory language and then to the legislative history if the statutory language is unclear.'" *Murphy v. Dalton*, 81 F.3d 343, 350 (3d Cir. 1996) (quoting *Blum v. Stenson*, 465 U.S. 886, 896, 79 L. Ed. 2d 891, 104 S. Ct. 1541 (1984)). As noted, COWPTA does not define "oil produced from tar sands," but "where Congress has used technical words or terms of art, it is proper to explain them by reference to the art or science to which they are appropriate." *Corning Glass Works v. Brennan*, 417 U.S. 188, 201 (1974) (internal quotation marks and alterations omitted). We ordinarily look to the meaning of a statutory term at the time the statute was adopted. *See MCI Telecomm. Corp. v. American Tel. & Tel. Co.*, 512 U.S. 218, 228, 129 L. Ed. 2d 182, 114 S. Ct. 2223 (1994) (explaining that "the most relevant time for determining a statutory term's meaning" is the time when the statute became law); *see also McDermott Int'l, Inc. v. Wilander*, 498 U.S. 337, 342, 112 L. Ed. 2d 866, 111 S. Ct. 807 (1991) (interpreting statute as of the date of its passage); *Perrin v. United States*, 444 U.S. 37, 42, 62 L. Ed. 2d 199, 100 S. Ct. 311 (1979) (same). In this case, the District Court did not rely on the industry understanding of "tar sand oil," in part because "the testimony offered at trial suggests that,

in fact, there was no industry consensus regarding a definition of tar sands in 1980 when Section 29 was enacted." *Shell*, 996 F. Supp. at 369.[9] Shell contests the court's factual finding and argues that, even in the absence of an industry consensus, the court should have limited itself to selecting among definitions that were acceptable to some petroleum experts in 1980.

A

Contending the District Court misunderstood its theory of the case, Shell contests the court's finding there was no consensus definition of "tar sand oil" in 1980. The District Court described Shell's definition of tar sand oil as

> any consolidated or unconsolidated rock (other than coal, oil shale, or gilsonite) that either: (1) contains a hydrocarbonaceous material with a gas-free viscosity, at original reservoir temperature, greater than 10,000 centipoise,[10] or (2) contains a hydrocarbonaceous material and is produced by mining or quarrying.

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[9] The Texaco Court, on a different record, found that "no single definition of tar sands was universally recognized" when COWPTA was enacted but that the industry "generally understood" the term to refer to oil too viscous to be produced economically using only primary production techniques. *Texaco*, 101 T.C. at 573.

[10] Within the petroleum industry, viscosity is measured in centipoise (cp). The viscosity of water is approximately 1 cp, while that of molasses is 7,000 cp.

Shell, 996 F. Supp. at 369. At trial, Shell referred to this definition as the "viscosity standard" and on appeal calls it the "quantitative standard." Shell concedes this standard was not generally accepted until 1983 but asserts that, in 1980, petroleum engineers agreed that "tar sand oil" was oil too viscous to be produced using primary production methods (the "primary production definition"). Furthermore, Shell maintains that petroleum experts in 1980 were able to identify tar sand and tar sand oil by inspection. Shell calls this experience-based identification of tar sand oil the "qualitative standard." According to Shell, the viscosity standard was a conservative quantification of the earlier primary production and qualitative definitions.[11] Because the trial court made no findings with respect to the other proposed definitions or their relationships to the viscosity standard,[12] Shell seeks a remand to determine whether the qualitative or the primary production definition was widely accepted by the industry in 1980 and whether the Potter Sands oil meets those definitions.

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[11] The *Texaco* court found the quantitative viscosity definition to be "consistent with the oil and gas industry's definition of tar sands as of April 1980," when COWPTA was enacted. *See Texaco*, 101 T.C. at 574.

[12] The District Court discussed the viscosity standard at length but did not mention the qualitative or primary production definitions. The court supported its finding that there was no consensus definition in 1980 with citations to testimony by a Shell expert and to a Shell Proposed Finding of Fact, *see Shell*, 996 F. Supp. at 369, which discussed the lack of agreement on a quantitative distinction between tar sand oil and heavy oil.

But Shell did not properly assert these additional industry definitions at trial. In the Pretrial Order, entered three days before trial, Shell listed only two "Issues of Law Which Remain to Be Litigated":

> (1) Whether the consensus definition of tar sand oil as having a viscosity greater than 10,000 centipoise, measured gas-free, at original reservoir temperature, identifies "oil produced from . . . tar sand" under 26 U.S.C. § 29 in 1983 and 1984?
>
> (2) Whether FEA ruling 1976-4 . . . has any utility in identifying "oil produced from . . . tar sand" under 26 U.S.C. § 29?

Shell Petroleum, Inc. v. United States, No. 93-508, slip op. at 15 (D. Del. Aug. 24, 1995) (Pretrial Order) (first and third ellipsis in original). The pretrial order controls the subsequent course of the trial unless modified to prevent manifest injustice. *See* Fed. R. Civ. P. 16(e); *Hassan v. Stafford*, 472 F.2d 88, 95 (3d Cir. 1973). This order was never modified, nor did Shell request a modification. Indeed, Shell's opening statement confirmed to the court its theory of the case:

> We will provide testimony that will show that the 10,000 centipoise definition of tar sand oil was the subject of considerable discussion, considerable thought among industry experts and knowledgeable Government officials prior to 1980 and in the--throughout the year, the early 1980's.
>
> And the point is here that, although tar sand experts knew what tar sands were, there was no precise and

generally acceptable demarcation between tar sand oil and other heavy oils.

The statement does not advance the theories Shell now proposes.

Shell has directed our attention to passages in the pretrial order, to passages in briefs submitted to the District Court, and to certain testimony elicited without objection at trial[13] in which it claims it raised its other definitions. Generally, pretrial orders are liberally construed to permit the parties to advance their cases, *see United States Gypsum Co. v. Schiavo Bros.*, 668 F.2d 172, 181 n.12 (3d Cir. 1981), and an issue can be tried by consent when testimony relevant to the issue is introduced without objection, *see Douglas v. Owens*, 50 F.3d 1226, 1236 (3d Cir. 1995). But a party still must unequivocally put its position before the trial court at a point and in a manner that permits the court to consider its merits. *See Keenan v. City of Philadelphia*, 983 F.2d 459, 471 (3d Cir. 1992) ("The crucial question regarding waiver is whether defendants presented the argument with sufficient specificity to alert the district court"); *Portis v. First Nat'l Bank*, 34 F.3d

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[13] Many of these passages are themselves not properly before us, because Shell has not included them in the appellate record. The appellant is required to provide a record to support the claims it makes on appeal. *See* Fed. R. App. P. 10(b), 11(a); *Scarfo v. Cabletron Sys., Inc.*, 54 F.3d 931, 963 (1st Cir. 1995); *Schmid v. United Bhd. of Carpenters*, 827 F.2d 384, 386 (8th Cir. 1987); *United States v. Hart*, 729 F.2d 662, 671 (10th Cir. 1984). Based on the excerpts Shell has quoted to us, the passages outside the appellate record on which Shell relies are no stronger than those in the record.

325, 331 (5th Cir. 1994) ("The raising party must present the issue so that it places the opposing party and the court on notice that a new issue is being raised."). We believe that Shell did not raise its primary production or qualitative definitions in an unequivocal manner.[14]

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[14] For instance, Shell noted in the section of the pretrial order entitled "Statement of What Plaintiffs Expects [sic] to Prove,"

> During 1980, the Viscosity Standard became DOE's standard for distinguishing between tar sand oil and other heavy oils. Prior to adoption of the Viscosity Standard in 1980, Defendant's agency DOE, and its predecessor the Bureau of Mines, relied on physical inspection of core and oil samples to identify tar sand. Shell's Potter Sands and the oil produced therefrom are tar sands and tar sand oils under the 1980 DOE practices.

In this passage, Shell asserted that DOE, but not the petroleum industry as a whole, identified tar sand using Shell's qualitative standard. Shell did not claim its Potter Sands oil satisfied the qualitative standard: it stated that its oil was tar sand oil according to "the 1980 DOE practices," an ambiguous phrase which could have referred either to the qualitative standard or to the quantitative viscosity standard, allegedly adopted in 1980. But statements made in the same section of the pretrial order suggest that Shell was advancing the quantitative standard at trial:

> Tar sand is rock containing crude oil with a viscosity exceeding 10,000 cp measured gas-free at original reservoir temperature. . . .
>
> The consensus of industry and the United States government in 1980 was that an agreed terminology for tar sands oil to adequately distinguish it from other heavy oils

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was needed. . . .

Here, Shell explicitly urges the quantitative standard on the court and acknowledges that the standards in use in 1980 were unacceptable to the consensus of petroleum experts. Even a liberal interpretation of this language will not embrace the position Shell takes on appeal.

Shell was more explicit in its post-trial proposed findings of fact and conclusions of law, stating, e.g., "The degree of viscosity of tar sand oil was commonly expressed as oil that could not be commercially produced through a wellusing primary recovery methods." Post-trial briefs are not generally appropriate places to raise one's theory of the case. In any event, this brief also fails to assert Shell's position clearly. The sentence just quoted was followed by an assertion that the industry shared "[a] common understanding that the line of demarcation at which tar sand oil became more viscous than heavy oil needed to be established quantitatively" and was contained in a section entitled, "The Court may consider the industry and government expert development of the 10,000 cp viscosity distinction between tar sand and other heavy oils in applying the earlier enacted 26 U.S.C. § 29 for 'oil produced from . . . tar sands'." Considering the post-trial findings of fact and conclusions of law in its entirety, we conclude Shell continued to assert the viscosity standard after trial.

As discussed *infra*, the testimony on which Shell relies could not support the factual findings Shell proposes to seek on remand. Furthermore, Shell explained to the District Court that the viscosity standard emerged in 1983 out of ongoing industry discussion. The evidence introduced regarding the pre-1983 standards was consistent with this background information regarding the development of the quantitative viscosity standard. Hence, neither the government nor the court had reason to believe Shell was

We have frequently noted "the well-established rule that absent compelling circumstances an appellate court will not consider issues that are raised for the first time on appeal." *Patterson v. Cuyler*, 729 F.2d 925, 929 (3d Cir. 1984).[15] "This general rule applies with added force where the timely raising of the issue would have permitted the parties to develop a factual record," because we cannot know on appeal what evidence the adverse party would have presented or brought out through cross-examination. *Harris v. City of Philadelphia*, 35 F.3d 840, 845 (3d Cir. 1994) (internal quotation marks omitted). Finding no "compelling circumstances" requiring consideration of Shell's theories, we decline to exercise our discretion to do so. *See American Bearing Co. v. Litton Indus.*, 729 F.2d 943, 949-50 (3d Cir. 1984).

Furthermore, our review of those portions of the record Shell has brought to our attention leads us to conclude that the possibility the District Court would find the facts as Shell describes them is remote. The strongest evidence Shell has cited comes from a report by its expert, Dr. Khalid Aziz, who wrote,

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raising a new theory of the case. *See Douglas*, 50 F.3d at 1236 ("An issue has not been tried by implied consent if evidence relevant to the new claim is also relevant to the claim originally pled, because the defendant does not have any notice that the implied claim was being tried.").

[15] Furthermore, to promote orderly trial procedures, appellate courts are sensitive to the importance of respecting the pretrial order on appeal. *See Correa v. Hospital San Francisco*, 69 F.3d 1184, 1195 (1st Cir. 1995).

Typically described [prior to 1980] as 'extremely viscous,' the tar sand oil was further depicted as oil that could not be produced commercially on primary production. The literature most commonly describes 'tar sand' as a naturally occurring rock formation containing a hydrocarbon so viscous that it cannot be economically produced through wells using only primary recovery methods.

But Dr. Aziz testified at trial,

Prior to 1980, I did not see that there was a consensus in the industry as far as a precise definition of tar sand was concerned . . . .

But by 1980 a consensus did start to build--did not reach a consensus point, but did start to build around the use of 10,000 centipoise. . . .

In 1983, the definition of tar sands oil was well-established as the viscosity base definition that we have been talking about, viscosity of greater than 10,000 centipoise at reservoir conditions on a gas-free basis. . . .

. . . .

[Before 1980, e]everyone knew that oils from tar sands were highly viscous. And I think people simply looked at the extreme and--looked at them as highly viscous, but they didn't know where to draw the line between tar sand oils and heavy oils. . . .

Dr. Aziz also confirmed at trial the accuracy of a statement he had written in his report: "In 1980 the phrase 'oil produced from tar sands' was commonly understood to mean all crude oil more viscous than heavy oil. However, there was no universally-accepted precise distinction between heavy oil and tar sand oil."

Similarly, Shell has called our attention to this testimony of a former DOE petroleum engineer:

> The general description that [DOE] used of tar sand [in 1979/1980] . . . was any rock containing a very viscous oil. And you could expand on that. In many cases we said it was too viscous to flow through the reservoir or to the well bore, or too viscous to be produced by primary recovery methods, for instance.

The witness was also asked how he identified tar sand when he first began working with it in 1970 and replied, "I looked at it and I knew it was tar sand." But on cross-examination, the witness agreed that "in the industry, as of April of 1980, there was no consensus definition of [sic] distinguishing heavy oil from tar sand oil." Because Shell's own experts testified there was no consensus definition of tar sand oil in 1980, it is unlikely Shell could prevail on remand. Where the possibility of a different outcome is remote, remand for consideration of factual issues not raised at trial is inappropriate. *See Hormel v. Helvering*, 312 U.S. 552, 558, 85 L. Ed. 1037, 61 S. Ct. 719 (1941).

B

Assuming no definition was universally accepted in the petroleum industry in 1980, Shell insists the District Court should have limited itself to selecting one of the definitions used by petroleum engineers at that time. In that regard, Shell argues the congressional record should have been consulted only for that limited purpose.

Reliance on expert definitions of terms of art is a sound "general rule of construction," *Massachusetts v. Blackstone Valley Elec. Co.*, 67 F.3d 981, 986 (1st Cir. 1995), but Shell has cited no authority supporting the proposition that, where no definition of a term of art is broadly accepted in the relevant technical field, a court is permitted only to choose among rival expert definitions. Where technical experts differ in their use of a term, the presumption that Congress has adopted an industry definition grows weaker and the courts will rely more heavily on other tools to ascertain Congress's meaning. Thus, in *Atlantic Mutual Insurance Co. v. Commissioner*, 523 U.S. 382, 118 S. Ct. 1413, 140 L. Ed. 2d 542 (1998), *aff'g* 111 F.3d 1056 (3d Cir. 1997), the Supreme Court considered a property and casualty insurer's challenge to the IRS's administrative interpretation of "reserve strengthening" as used in the Tax Reform Act of 1986 § 1023(e)(3)(B), reprinted in note following 26 U.S.C.A. § 846 (West 1988). After concluding, based on a review of the expert testimony at trial, that the term had no established meaning in the field of property and casualty insurance, the Court accorded Chevron deference to the agency regulation without further reference to insurance industry usage. *See Atlantic Mutual*, 118 S. Ct. at 1417-18. Here, there is no agency interpretation to defer to, but we rely on traditional

tools of statutory interpretation in adopting the DOE definition.[16]

III

We believe the definition of "tar sand oil" in DOE Ruling 1976-4 is the one most compatible with congressional intent. As noted, Title I of COWPTA defines oil produced using enhanced extraction techniques as crude oil. Shell's definition, on the other hand, would categorize oil produced using enhanced extraction techniques as tar sand oil. Congress clearly distinguished tar sand oil from crude oil and considered tar sand oil a crude oil substitute. Because oil produced using enhanced extraction techniques, such as Shell's Potter Sands oil, is not a crude oil substitute, it could not qualify for the nonconventional source tax credit. Furthermore, Shell's definition would categorize crude oil produced with technologies widely available when COWPTA was enacted as tar sand oil. But Congress enacted the nonconventional source credit to encourage the development of new technologies that would produce crude oil alternatives.

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[16] We note that in appropriate cases the Supreme Court has looked to the legislative record to confirm that Congress intended to adopt the technical definition of a term of art, *see Louisiana Publ. Serv. Comm'n v. FCC*, 476 U.S. 355, 371-73, 90 L. Ed. 2d 369, 106 S. Ct. 1890 (1986); *Corning Glass Works*, 417 U.S. at 198-201, or has declined to accept a trade definition that conflicted with the legislative history, *see Idaho Metal Works v. Wirtz*, 383 U.S. 190, 199-205, 15 L. Ed. 2d 694, 86 S. Ct. 737 (1966).

A

As noted, Shell's Potter Sands oil was produced through steam injection, an enhanced (or tertiary) recovery method. As the District Court's reading of the statute demonstrated, oil produced using tertiary recovery methods (which the statute calls "tertiary oil"), is crude oil subject to the windfall profit tax imposed in Title I. *See Shell*, 996 F. Supp. at 370.[17] Shell

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[17] For tax purposes, Congress divided crude oil into three tiers. See 26 U.S.C. § 4991(c)-(e). Tier 1 oil was taxed at the highest rate, tier 3 at the lowest. *See id.* §§ 4987(b)(1), (3). Tier 3 oil included "incremental tertiary oil," *id.* § 4991(e)(4), defined (with qualifications and adjustments not relevant here) as the difference between the amount of oil produced in a month from a property using a "tertiary recovery project" and the average monthly oil production from that property prior to passage of the Act, *id.* § 4993(a)-(b). As we understand this provision, all oil produced from a tertiary recovery project is tertiary oil, and any increase in production after the Act was passed is incremental tertiary oil. *Cf.* 10 C.F.R. § 212.78(c) (1980) (defining "incremental crude oil"). Tertiary recovery projects are those employing "tertiary recovery methods," *see* 26 U.S.C. §§ 4993(c)(1)(B), (c)(2)(A), which include "steam drive injection" and "cyclic steam injection," *id.* § 4993(d)(1), 10 CFR § 212.78(c) (1979). The District Court found, and Shell does not contest, that these are the procedures Shell used at Potter Sands. *See Shell*, 996 F. Supp. at 370 & n.4.

It is clear that all tertiary oil, and not just incremental tertiary oil, is taxable crude oil. There is no chemical distinction between incremental and non-incremental tertiary oil and the statute specifies no way to identify the incremental or non-incremental "part" of a month's production. Furthermore, if non-incremental tertiary oil were not crude oil, it would not be subject to the windfall tax, *see*

does not dispute this conclusion. But Shell contends that tertiary oil can be classified as both crude oil and tar sand oil, arguing that its Potter Sands oil, extracted through enhanced (tertiary) recovery methods, is also tar sand oil eligible for the Title II tax credit. Relying on the legislative history, the District Court found that Congress did not consider crude oil to be tar sand oil, nor would Congress have imposed an excise tax and granted a tax credit to the same type of oil in the same statute. Because Shell's Potter Sands oil was indisputably crude oil subject to the windfall profit tax, we hold, like the
District Court, it cannot also be tar sand oil eligible for the tax credit.

1

On this point, the legislative history is instructive. In its report on Title I (imposing the windfall profit tax), the Senate Finance Committee specified, "The term 'crude oil' . . . applies only to natural crude petroleum and does not include synthetic petroleum, such as oil from shale or tar sands." S. Rep. No. 96-394, at 56, reprinted in 1980 U.S.C.C.A.N. at 465. The Conference Committee similarly explained, "The term 'crude oil' . . . does not apply to synthetic petroleum such as oil production from shale or tar sands." H.R. Conf. Rep. No. 96-817, at 114 (1980), reprinted in 1980 U.S.C.C.A.N. 642, 667. Based on this legislative history, the

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26 U.S.C. §§ 4986(a), 4991(a), in which case only increases in production of tertiary oil would be taxed, contrary to Congress's intent to stimulate new oil production, *see* S. Rep. No. 96-394 at 27, reprinted in 1980 U.S.C.C.A.N. at 437.

District Court concluded, "Congress explicitly distinguished crude oil from tar sands, and understood tar sands to be a crude oil substitute." *Shell*, 996 F. Supp. at 370; *accord Texaco*, 101 T.C. at 579. Because Congress specified that oil extracted using enhanced production techniques is crude oil, oil extracted using enhanced production techniques cannot be tar sand oil, a crude oil substitute.

Shell contends this legislative history should be interpreted in light of expert testimony that tar sand oil in its natural state is not synthetic oil but rather crude oil that can be processed into synthetic oil. But the clear import of the Committees' Reports is that all oil produced from tar sands is synthetic petroleum, not crude oil. Furthermore, because only crude oil is subject to the windfall profit tax, *see* 26 U.S.C. §§ 4986(a), 4991(a), the intent behind the Committee Reports is to exempt tar sand oil from the tax by specifying that it is not crude oil. But according to Shell, the processing of tar sand oil into synthetic oil is generally unnecessary in the continental United States.[18] Shell has proposed no reason why Congress would exempt from the windfall profit tax the production of tar sand oil that is later processed into synthetic oil if the processing serves no useful purpose in important oil-producing parts of the country. Finally, it is worth noting that the Federal Energy Agency, in Ruling 1976-4, spoke of tar sand oil as a "so-called synthetic fuel[ ] (or crude oil substitute)." 10 C.F.R. ch. II Rulings at 371. This language supports the view

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[18] Shell has represented, citing the testimony of its experts, that tar sand oil is refined into synthetic crude oil primarily to permit it to flow through pipelines in cold weather, and that such refining is rare in the continental United States because of our warmer climate.

that, when COWPTA was enacted, tar sand oil was not generally considered to be crude oil, subject to the windfall profit tax.

The District Court concluded that Congress did not regard oil capable of extraction through enhanced production methods as tar sand oil when COWPTA was enacted. We agree. The statute establishes that tertiary oil (oil extracted with enhanced production methods) is a type of crude oil, but Congress, like the FEA, did not consider tar sand oil to be crude oil. Therefore, tertiary oil cannot be tar sand oil. As the District Court explained, under Shell's interpretation, tertiary oil (oil produced by enhanced recovery methods)

> would be taxed as crude oil and, therefore, excluded from the category of tar sands. That same oil, however, would be defined as tar sands under Section 29 according to Shell's definition. This would result in two different definitions of tar sands under Title I and Title II. Clearly, this was not the intent of Congress.

Shell, 996 F. Supp. at 370-71 (footnote omitted).[19] Because

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[19] Similarly, the Texaco court explained that, under the definition Shell now advances,

> high viscosity crude oil produced using secondary and enhanced oil recovery methods would be characterized as crude oil (which does not include oil from tar sands) for purposes of title I, while the same high viscosity crude oil would be characterized as oil produced from tar sands for purposes of title II. While the reference to tar sands in defining crude oil for purposes of title I is not

Shell does not contest the District Court's finding that its Potter Sands oil is tertiary oil, Shell's oil cannot be tar sand oil eligible for the tax credit.

2

The logic and structure of the act also demonstrate that crude oil is not tar sand oil. If oil producible using enhanced recovery methods, including the oil produced at Potter Sands, were classified both as crude oil and as tar sand oil, it would be subject to the windfall profit tax and also eligible for the nonconventional source tax credit. The District Court declined to interpret the statute this way "absent some evidence that Congress intended such an anomalous result." *Shell*, 996 F. Supp. at 371. We agree. *See United States v. McKie*, 36 V.I. 367, 112 F.3d 626, 631 (3d Cir. 1997) (discussing courts' "obligation to construe statutes sensibly and avoid constructions which yield absurd or unjust results").

Shell defends its interpretation by pointing out that under COWPTA the windfall profit tax was phased out as the price of oil fell whereas the nonconventional fuels credit was phased in under the same conditions. Shell suggests that the tax collected in years when oil prices were high was to be used to finance the subsidy when oil prices fell. Essentially,

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determinative in defining tar sands for purposes of title II, we do not think that Congress would have used the term "tar sands" in fundamentally different ways within the same legislative enactment without clearly expressing an intent to do so.

101 T.C. at 580.

Shell suggests that the tax and credit together functioned as a rough-and-ready producer price stabilization scheme. But the legislative record is devoid of any suggestion that Congress intended such a result. Instead, the Senate Finance Committee explained that the Act "uses a large part of the revenue from the windfall profit tax to finance tax incentives for a wide range of alternate sources of energy." S. Rep. No. 96-394, at 8, reprinted in 1980 U.S.C.C.A.N. at 419. It appears Congress wanted to transfer windfall crude oil profits to producers of a distinct, "alternate," class of energy sources. Furthermore, Shell concedes that, on its reading of the statute, oil produced from Potter Sands would have received both a tax and a credit in 1981 and 1982. If Congress had sought to stabilize producer prices for tar sand oil, we do not see why

Congress would have imposed a tax and provided a subsidy in the same year.[20] Therefore, we believe the District Court correctly found that Congress did not intend to classify the same oil as both taxable crude oil and tar sand oil eligible for the tax credit. Since oil produced using enhanced recovery methods, such as Shell's, was subject to the windfall profit tax, it cannot have been eligible for the nonconventional source tax credit.

3

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[20] We note that Congress provided targeted subsidies to tertiary oil in Title I by taxing increases in tertiary production at the lower, tier 3 rate, *see supra* n.17, and exempting altogether oil sold to finance tertiary extraction projects by independent producers, *see* 26 U.S.C. §§ 4991(b)(4), 4994(c)(1), (c)(4)(A), (c)(4)(D); 10 C.F.R. § 212.78 (1980); H.R. Conf. Rep. No. 96-817, at 93, reprinted in 1980 U.S.C.C.A.N. at 646.

In summary, Shell's proposed definition, unlike DOE's, would classify oil producible through enhanced recovery techniques as tar sand oil. Because this classification would be contrary to the statutory scheme and to congressional intent, the District Court properly adopted the definition from DOE Ruling 1976-4.

B

Congress's explanation of the purpose of COWPTA provides further reason to reject Shell's proposed definition. As noted, Shell obtained crude oil from Potter Sands using technologies already well established in 1980. But the alternative fuel production credit was added by the Senate Finance Committee "to encourage energy conservation and production of alternate energy sources." S. Rep. No. 96-394, at 6, reprinted in 1980 U.S.C.C.A.N. at 417. "These alternative energy sources," the Committee explained, "typically involve new technologies, and some subsidy is needed to encourage these industries to develop to the stage where they can be competitive with conventional fuels. The information gained from the initial efforts at producing these energy sources will be of benefit to the entire economy." *Id.* at 87, reprinted in 1980 U.S.C.C.A.N. at 496. Because continued use of a widely available means of crude oil production is not an "initial effort[ ]" that will stimulate the development of new energy technologies, we agree with the District Court that oil producible with tertiary extraction methods available in 1980, such as steam injection, does not qualify for the nonconventional source credit. *See Shell*, 996 F. Supp. at 367 ("Domestic crude oil would not logically be categorized as an alternative energy source. . . . Rather, [Congress] endeavored to credit the production of alternative

fuels or so-called crude oil substitutes."); *accord Texaco*, 101 T.C. at 577 ("Section [29] was not intended to subsidize the production of crude oil but, to the contrary, was intended to encourage the development of crude oil substitutes.").

Shell maintains the District Court imposed a "new technologies" requirement not found in the statute on those seeking the tax credit. We disagree. The energy sources eligible for subsidy are those specified in 26 U.S.C.A. § 29 (c)(1). Many of those sources were defined by Congress. *See id.* § 29(c)(2)-(3); H.R. Conf. Rep. No. 96-817, at 138-41, reprinted in 1980 U.S.C.C.A.N. at 689-93; S. Rep. No. 96-394 at 87-88, reprinted in 1980 U.S.C.C.A.N. at 496-97. So long as the energy produced is of one of the specified types, the taxpayer is eligible for the credit, whether or not the taxpayer used new technology. But where the definition of an energy source is unclear, Congress's directive that the eligible energy sources to be subsidized "typically involve new technologies " assists us in interpreting the provision. Congress's intent is best implemented through the DOE definition, which excludes energy sources produced with technologies already widely used or exploited when the Act was passed.

IV

In this case, as the District Court noted, "the definition of 'tar sands' contained in the [DOE] Ruling is completely congruous with Congress' intent to both encourage the development of new technologies and limit the Section 29 credit to crude oil substitutes that could not be obtained using conventional methods." *Shell*, 996 F. Supp. at 367. Shell points out that the DOE Ruling was issued in response to

"inquiries with respect to the applicability of the [EPAA price and supply controls] to the so-called synthetic fuels (or crude oil substitutes) processed from . . . tar sands . . . and other natural deposits that must be mined before the crude oil substitute can be extracted." DOE Ruling 1976-4, 10 C.F.R. ch. II Rulings at 371. Shell interprets this language to mean that FEA had received inquiries involving only tar sand oil that was both extracted from mined tar sand and processed into synthetic crude oil. Shell argues that FEA adopted an artificially narrow definition of "tar sands" in order to ensure that its Ruling would exclude only such oil from EPAA regulation. We are not convinced. It seems unlikely that FEA would have knowingly propounded an inaccurate definition, even for a limited purpose, rather than simply specifying that its Ruling applied only to tar sand oil that is extracted from mined tar sand and processed into synthetic crude oil. We note that the Ruling's definition does not limit tar sands oil to oil extracted from tar sands after mining. Therefore we agree with the District Court in adopting the DOE Ruling's definition of tar sands for purposes of the nonconventional fuels tax credit.[21]

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[21] Shell also argues that Ruling 1976-4 is too obscure to be relied on in defining "oil produced from tar sands." But the statute adopted certain definitions contained in the EPAA regulations, such as "stripper well," "newly discovered oil," "qualified tertiary recovery project," "tertiary recovery method," "tertiary incentive revenue," "allowed expenses" (in certain contexts), "front-end oil," "front-end tertiary project," and "crude oil", see 26 U.S.C. §§ 4991(d)(1)(A), (e)(2), 4993(c)(1)(A), (d)(1)(A), 4994(c)(2)(C), (c)(3)(A), (c)(4)(B), (c)(4)(D), 4996(b)(1), (b)(8) and also specified that the "base level" used in defining incremental tertiary oil is to be "determined under rules similar to" EPAA regulations, *see id.*

V

For the foregoing reasons, we will affirm the judgment of the District Court.

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§ 4993(b)(1). In its report on the bill, the Senate Finance Committee wrote, "Reference to the energy regulations also would be important when the Secretary or producers must make determinations by analogy to the energy regulations, e.g., computing the base level for a tertiary project," S. Rep. No. 96-394 at 57, reprinted in 1980 U.S.C.C.A.N. at 466-67, and endorsed administrative interpretations of the regulations, *see id.*, reprinted in 1980 U.S.C.C.A.N. at 467. We give due regard to Ruling 1976-4, a DOE interpretation of the EPAA regulations, in applying 26 U.S.C. § 29.

APPENDIX F

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF DELAWARE

Civil Action No. 93-508-JJF

[Filed October 16, 1997]

SHELL PETROLEUM, INC. and SUBSIDIARY CORPORATIONS,
Plaintiff,

v.

UNITED STATES OF AMERICA,
Defendant.

Joseph J. Farnan, Jr., Chief Judge.

MEMORANDUM OPINION

I. BACKGROUND

This is an action brought by Plaintiff, Shell Petroleum Inc. ("Shell"), pursuant to 26 U.S.C. § 7422 for the refund of claimed overpaid federal income taxes and interest due thereon under 26 U.S.C. § 6611. Shell is incorporated under the laws of the State of Delaware and maintains a principal

office in Delaware at 1105 Market Street, Wilmington, Delaware, 19899. (D.I. 296 at ¶ 2(a)). Shell is the common parent of an affiliated group of corporations (the "Shell Affiliated Group"). The Shell Affiliated Group files consolidated federal income tax returns, and their taxable year is the calendar year. (D.I. 342 at 1, ¶ 4).

On May 15, 1991, Shell timely filed claims for a refund of the Shell Affiliated Group's 1983 and 1984 consolidated federal income taxes with the Internal Revenue Service ("the IRS"). (D.I. 296 at ¶ 2(c)). On its 1983 and 1984 Amended Returns, Shell claimed credits against 1983 and 1984 federal income taxes for oil recovered from its Midway Sunset Oil Field in Kern County, California, pursuant to 26 U.S.C. § 29. (D.I. 296 at ¶ 2(c)); (D.I. 296 at 5, ¶ 9). Shell claimed tax credits of $ 1,690,902 for 1983 and $ 3,660,248 for 1984. (D.I. 296 at 24). The IRS denied Shell's refund claims, and thereafter Shell timely filed a complaint in this Court on October 29, 1993, asserting counts consistent with the refund claims. (D.I. 296 at ¶ 2(c)).

Jurisdiction is conferred upon the Court by 26 U.S.C. § 7422 and 28 U.S.C. § 1346(a)(1). A bench trial was held on this matter, and this Memorandum Opinion shall constitute the Court's Findings of Fact and Conclusions of Law.

II. THE BASIS OF THE LAWSUIT

Pursuant to Title 26, Section 29 of the Internal Revenue Code, oil companies are eligible for an income tax credit of $ 3.00 for each barrel of "oil produced from ... tar sands." 26 U.S.C. § 29(c)(1)(A). Section 29, however, does not define the term "tar sands." The Government argues that the

appropriate definition of "tar sands" is found in Federal Energy Administration Ruling 1976-4 ("the FEA Ruling"), which defines tar sands as:

> The several rock types that contain an extremely viscous hydrocarbon which is not recoverable in its natural state by conventional oil well production methods including currently used enhanced recovery techniques.

41 Fed. Reg. 25886 (1976). Shell contends that the proper definition for "tar sands" as used in Section 29 results from a consensus developed in the petroleum industry that oil produced from tar sand is oil with a viscosity[1] greater than 10,000 centipoise, measured gas-free, at original reservoir temperature ("the Viscosity Standard"). (D.I. 342 at 23-24). The parties agree that if the Court determines that the FEA Ruling definition of "tar sands" is to be applied when interpreting Section 29, judgment should be entered for the Government. (D.I. 255 at 16, n.44). On the other hand, if the Court determines that the FEA Ruling definition does not apply to Section 29, the Court must then determine whether Shell's proposed 10,000 centipoise standard is a universally accepted industry definition of "tar sands." If the Court

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[1] Viscosity is the measure of a fluid's resistance to flow. (D.I. 296 at 4). In an oil reservoir, viscosity is the measure of the oil's resistance to movement through the reservoir rock to the well-bore. (D.I. 296 at 4). Given uniform pressure and rock properties, a more viscous oil will move through the reservoir more slowly than a less viscous oil. Viscosity is measured in "poise." (D.I. 296 at 4). Oil field viscosity is usually stated in centipoise ("cp"). (D.I. 296 at 4).

accepts the industry's definition, it must also decide when that standard became the accepted industry definition of "tar sands" and whether Shell has in fact proven that the oil samples taken from its fields in the Potter Sands have a viscosity greater than 10,000 centipoise.

III. HISTORICAL BACKGROUND

In the early 1970's, the United States experienced a series of crises related to the country's oil supplies. These crises resulted from instability in international oil markets which in turn caused severe fluctuations in the price of imported oil. In an effort to alleviate these crises, the federal government enacted a series of extensive regulations.

The first energy crisis occurred in October, 1973, in the wake of the Arab-Israeli War, when the Organization of Petroleum Exporting Countries ("OPEC ") imposed an oil embargo on western countries, including the United States. Gary D. Allison, Energy Sectionalism: Economic Origins and Legal Responses, 38 Sw. L.J. 703, 705 (1984). The embargo, followed by a cartel pricing strategy, caused world oil prices to quadruple in less than a year and plunged numerous western economies into a cycle of inflation and recession. *Id.*

A. The Emergency Petroleum Allocation Act of 1973

On November 27, 1973, in response to the increased price of world oil, the United States Congress enacted the Emergency Petroleum Allocation Act ("EPAA"). *See* 15 U.S.C. §§ 751-760. The EPAA mandated that the President promulgate regulations providing for the mandatory allocation of crude oil, residual fuel oil, and each refined petroleum

product, at specified prices and amounts. 15 U.S.C. § 753(a).

While the price control system became increasingly complex, its two main components were "price ceilings" and "entitlement" payments. First, the EPAA set various price ceilings for two classifications of domestically produced oil. Proposed Windfall Profit Tax and Creation of Energy Trust Fund: Hearings Before the Committee on Ways and Means, No. 96-34, at 15-16 (1979) (hereinafter "Hearing"). Second, to prevent disparity in prices for crude oil from upsetting the competitive balance among regions of the country and within the oil refining industry, the EPAA used an "entitlement" system to equalize the costs of crude oil to all refiners. *Id.* at 16. Under this system, refineries were required to make "entitlement" payments to each other to ensure that each refinery paid the same average price for a barrel of oil, regardless of whether the oil was imported or domestically produced. *Id.* As a result, refiners who purchased more expensive imported oil were compensated by refiners who purchased domestically produced oil, which was less expensive due to the aforementioned price ceilings. *Id.* In effect, refiners who purchased less expensive domestic oil were required to subsidize competitors who purchased more expensive imported oil.

While the purpose of the EPAA was to "deal with shortages of crude oil, residual fuel oil, and refined petroleum products" in such a way as to "minimize the adverse impacts of such shortages ... on the American people and the domestic economy," it had the opposite effect. *Id.*; 15 U.S.C. § 751(b). Because the-price of domestic oil was controlled by the EPAA's price ceilings, the incentive to produce domestic

oil was removed. Hearing, *supra*, at 16. Consequently, there was
incentive for oil companies to import more expensive foreign oil. Therefore, as a result of the price controls and entitlement payments, the EPAA regulations encouraged oil consumption and importation and discouraged domestic oil production and the development of new energy sources.

B. The FEA Definition of Tar Sands

In 1976, the Federal Energy Administration ("FEA") received several inquiries with respect to whether the so-called "synthetic fuels," fuels processed from oil shale, tar sands, coal, and other natural deposits that must be mined before the crude oil substitute can be extracted, were subject to the price controls of the EPAA. FEA Ruling 1976-4, 41 Fed. Reg. 25886 (1976). In response to these inquiries, the FEA issued Ruling 1976-4, which announced the definition of tar sands that the Government relies upon in the instant action. FEA Ruling 1976-4 defines tar sands as

> the several rock types that contain an extremely viscous hydrocarbon which is not recoverable in its natural state by conventional oil well production methods including currently used enhanced recovery techniques.

Id. at 25886.

In rendering its decision, the FEA determined that Congress intended the EPAA price controls to apply only to fuel resources that were threatened to be in short supply. *Id.* The FEA reasoned that Congress could not have intended to

extend price controls to crude oil substitutes because crude oil substitutes were not being commercially produced when the EPAA was enacted. *Id.*

C. Titles I and II of the Crude Oil Windfall Profit Tax Act of 1980

As a result of the Iranian Revolution which halted Iranian oil exports for three months, the United States faced its second energy crisis in 1979. *Allison*, *supra*, at 706. Due to the reduction in Iranian oil production, world oil prices doubled, creating an economic shock even more severe than that experienced in 1973. *Id.* This price increase for imported oil further enlarged the gap between the cost of world oil and the cost of price-controlled domestic oil.

In April 1979, the Carter Administration announced its intention to exercise its discretionary authority and phase out the domestic oil price controls between June 1, 1979 and September 30, 1981, the date the EPAA regulations were to expire. H.R. Rep. No. 96-304, at 4 (1979), reprinted in 1980 U.S.C.C.A.N. 587, 591. In May 1979, shortly before the start of the phased decontrol, lower tier domestic oil was controlled at an average price of $ 5.91 per barrel and upper tier domestic oil at an average price of $ 13.02 per barrel. *Id.* At the same time, the average price of uncontrolled world oil, to which the price of both lower tier and upper tier oil was expected to rise as the price controls were phased out, was approaching $ 30 per barrel. *Id.* Therefore, the decontrol of domestic oil prices was expected to cause a significant increase in revenues received by oil producers and royalty owners. *Id.* at 7.

In response to the enormous increase in revenues that oil companies were expected to experience due to the price control phaseout, Congress enacted the Crude Oil Windfall Profit Tax Act ("COWPTA") of 1980. Under Title I of COWPTA, a Windfall Profit Tax ("WPT") was imposed on each barrel of domestically produced crude oil to supplement the decontrol of oil prices. 26 U.S.C. §§ 4986-4997 (repealed 1988). The purpose of the tax was to prevent oil companies and royalty owners from experiencing exceptional profits due to the phase out of price controls, while passing the increased oil cost to the consumer. S. Rep. No. 96-394, at 2 (1979), reprinted in 1980 U.S.C.C.A.N. 410, 414. The tax rate imposed ranged from 30 to 70 percent of the windfall profit realized as a result of price decontrol, depending on the type of oil produced. 26 U.S.C. § 4987 (b)(1)-(3) (repealed 1988). To encourage greater production of domestic oil, the tax exempted newly discovered oil, incremental production oil, and the first 1,000 barrels per day of stripper oil produced by independent producers. S. Rep. No. 96-394, at 1-2, 1980 U.S.C.C.A.N. at 413-14.

In its report discussing the Windfall Profit Tax, the United States Senate Finance Committee discussed the creation of business energy incentives. *Id.* at 3. The report stated that the Finance Committee sought to provide "significant tax incentives to encourage businesses to conserve energy and produce alternative sources of energy." *Id.*

To further this end, the report contained a provision specifically aimed at providing an alternative fuel production tax credit. *Id.* at 3. The $ 3.00 per barrel tax credit for "producing fuel from a nonconventional source" was codified in 26 U.S.C. § 29, Title II of COWPTA, and extended to "oil

produced from ... tar sands." 26 U.S.C § 29(c)(1)(A).[2] Title II of COWPTA provided for the use of its revenue to encourage energy conservation, promote production from alternate energy sources and ease the burden of higher energy prices on lower-income households. S. Rep. No. 96-394 at 27, 1980 U.S.C.C.A.N. at 437.

IV. THE PARTIES' CONTENTIONS

A. Shell's Position

Shell argues that the definition of the term "tar sands" as used in Section 29 is a question of fact. (D.I. 255 at 10). In support of its position, Shell argues that neither Section 29 nor the legislative history explicitly define "tar sands" and that the term does not have clear meaning to a layperson, but does have a particular meaning within the petroleum industry. (D.I. 255 at 10-11). Shell asserts that the Court cannot be expected to have specialized petroleum industry knowledge, and therefore, expert testimony is admissible to assist the Court in determining an accurate definition. (D.I. 255 at 11).

At trial, Shell offered expert testimony that in 1983 and 1984 the consensus industry definition of tar sands was crude oil with a viscosity greater than 10,000 centipoise measured gas-free at original reservoir temperature. (D.I. 255 at 8); (D.I. 307, Aziz at B-88). Shell argues that this industry definition is practical, administratively feasible and the

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[2] Section 29 was originally enacted in 1980 as Section 44D, and redesignated as Section 29 in the Deficit Reduction Act of 1984, Pub. L. No. 98-369, 98 Stat. 494, 826.

product of a consensus building among the petroleum industry's best technical experts that began years before Section 29 was enacted. (D.I. 255 at 8).

Shell further argues that the industry definition of tar sands is in consonance with the Congressional intent of the Section 29 tax credit. (D.I. 342 at 63). Shell asserts that the legislative history of Section 29 establishes that the purpose of the tax credit was to increase domestic oil production by encouraging the development of "alternative energy sources" and did not require investment in new technology. (D.I. 342 at 63). On this point, Shell argues that prior to the enactment of the tax credit, high viscosity tar sand oil was not commercially produced because its production costs were higher than those of conventional crude oil. (D.I. 342 at 64). Shell argues that by virtue of the tax credit, tar sands became competitive with conventional oil and enabled oil companies to commercially produce tar sand oil. (D.I. 342 at 64). Therefore, Shell contends that high viscosity tar sand oil constitutes an "alternative energy source" because it was not commercially produced prior to the enactment of Section 29. (D.I. 342 at 65). Lastly, Shell argues that extending the Section 29 tax credit to high viscosity tar sand oil fulfills Congressional intent to increase domestic oil production and reduce the nations dependence on imported oil. (D.I. 342 at 63).

B. The Government's Position

The Government argues that the definition of "tar sands" is a legal question and exclusively a judicial determination. (D.I. 334 at 50). Because the definition is a legal question, the Government argues that the Court should not consider the

expert testimony of petroleum engineers, but should limit its consideration to the plain meaning of the language of the statute and its legislative history. (D.I. 246 at 16).

The Government asserts that the statutory language and legislative history of Title I of COWPTA, which imposes the $ 3.00 per barrel excise tax on domestically produced crude oil, provides sufficient evidence for the Court to conclude that Congress intended the FEA Ruling to define tar sands for the purposes of the Section 29 tax credit. (D.I. 334 at 52). According to the Government, Title I of COWPTA subjected all nonexempt domestic crude oil to the WPT, and defined "crude oil" as having "the meaning given to such term by the June 1979 energy regulations." (D.I. 246 at 23). Therefore, the Government asserts that COWPTA incorporated the 1919 energy regulation promulgated by the Department of Energy ("DOE") and its predecessor the FEA. (D.I. 246 at 23). Additionally, both the House and Senate conference reports explicitly state that "it is anticipated that the Secretary will give due consideration to the various administrative rulings and judicial decisions which have interpreted or which construe those regulations." (D.I. 246 at 23 (citing H. R. Rep. No. 96-304, at 36 (1979); S. Rep. No. 96-394, at 56 (1979)). The Government interprets these statements as establishing congressional intent to draw the definitions of terms contained in COWPTA from FEA regulations and rulings and that at the time Congress passed COWPTA the only definition of tar sands for purposes of the June 1979 energy regulations was the FEA Ruling. (D.I. 246 at 23).

The Government argues that the EPAA, the price control phase out, and Titles I and II of COWPTA constitute an integrated statutory scheme dealing with the country's oil

production. (D.I. 334 at 71). More specifically, the Government asserts that the WPT, Title I of COWPTA, was enacted to address the windfall profits created by the phase out of the price controls created under the EPAA. (D.I. 334 at 71). Further, the Government argues that the WPT mandated that the revenues from the tax be used to fund various energy programs, including the income tax credits contained in Title I of COWPTA, and that Section 29 is part of Title II of COWPTA. (D.I. 334 at 71). Consequently, the Government contends that because Title I and Title II are part of an integrated statutory scheme aimed at regulating aspects of the oil industry, the definition of a term used in Title I must also apply to the same term used in Title II. (D.I. 334 at 72). Pursuant to this reasoning, the Government argues that the definition of "tar sands" articulated in FEA Ruling 1976-4 applies to the term "tar sands" as used in Section 29.

The Government also asserts that the legislative history of Section 29 establishes that the tax credit was intended for oil companies who developed new technologies in an effort to discover alternative sources of energy. (D.I. 334 at 54). According to the Government, the tar sands definition contained in the FEA Ruling is consistent with Congressional intent to promote new oil production technology because it excludes from the Section 29 tax credit oil produced by conventional oil well production methods, including currently used enhanced recovery techniques (production methods that were already in use within the petroleum industry when the credit was enacted). (D.I. 334 at 58-60).

V. STANDARD OF REVIEW

In a tax refund suit, the taxpayer bears the burden of

proving that it is entitled to a refund. *United States v. Janis*, 428 U.S. 433, 440, 49 L. Ed. 2d 1046, 96 S. Ct. 3021 (1976); *Sullivan v. United States*, 618 F.2d 1001, 1008-09 (3d Cir. 1980); *Tunnell v. United States*, 512 F.2d 1192, 1194 (3d Cir.), *cert. denied* 423 U.S. 893, 46 L. Ed. 2d 124, 96 S. Ct. 190 (1975). For the reasons discussed below, the Court finds that Shell has not met its burden in this case.

VI. DISCUSSION

The Court concludes that the definition of "tar sands" under Section 29 is a question of law, and the definition contained in FEA Ruling 1976-4 and advanced by the Government in this case is applicable for the purposes of COWPTA. The Court bases its decision on three factors: 1) statutory interpretation and legislative intent; 2) the unworkability of the definition advanced by Shell; and 3) the reasoning of the Tax Court in *Texaco Inc. v. Commissioner of Internal Revenue*, 101 T.C. 571 (1993).

A. Statutory Interpretation and Legislative Intent

Statutory interpretation is a question of law reserved for the Court. *McDermott Int'l, Inc. v. Wilander*, 498 U.S. 337, 356, 112 L. Ed. 2d 866, 111 S. Ct. 807 (1991). The Court's main objective in interpreting any statute is to determine what Congress meant by the use of the statutory language being construed. *United States v. American Trucking Ass'ns*, 310 U.S. 534, 542, 84 L. Ed. 1345, 60 S. Ct. 1059, *reh'g denied* 311 U.S. 724, 85 L. Ed. 472, 61 S. Ct. 53 (1940); *Helvering v. Stockholms Enskilda Bank*, 293 U.S. 84, 93-94, 79 L. Ed. 211, 55 S. Ct. 50 (1934); *Sperling v. Hoffmann-La Roche*, 24 F.3d 463, 470 (3d Cir. 1994). Where statutory language is

ambiguous, the Court may look to legislative history and to the reasons for the statute's enactment. *American Trucking*, 310 U.S. at 543-544; *Atlantic Mut. Ins. Co. v. Commissioner of Internal Revenue*, 111 F.3d 1056, 1057, 1062 (3d Cir. 1997). If the legislative history indicates the meaning of a statutory term, courts will reject the application of expert testimony to define the term. *Principal Mut. Life Ins. Co. v. United States*, 26 Cl. Ct. 616, 624-25 (1992), modified on other grounds, 29 Fed. Cl. 157 (1993), *aff'd*, 50 F.3d 1021, 1995 WL 114783 (Fed. Cir. 1995); *American Nat'l Insurance Co. v. United States*, 231 Ct. Cl. 604, 690 F.2d 878, 888 (Cl. Ct. 1982).

Preliminarily, it is noted that the title of an act may shed light on the intended meaning of a statute, *Maguire v. Commissioner of Internal Revenue*, 313 U.S. 1, 9, 61 S. Ct. 789, 85 L. Ed. 1149 (1941). Section 29 is entitled "Credit for Producing Fuel From a Nonconventional Source." This title provides an initial indication of Congress' intent to promote the use of new or atypical sources of fuel.

Exploration of the legislative history of COWPTA reveals the congressional intent to encourage the development of alternative sources of energy. In its 1979 report to Congress, the Senate Finance Committee stated its belief that "a tax credit for the production of energy from alternative sources will encourage the development of these resources . . . These alternative energy sources typically involve new technologies, and some subsidy is needed to encourage these industries to develop to the stage where they can be competitive with conventional fuels." S. Rep. No. 96-394 at 87 (emphasis added), 1980 U.S.C.C.A.N. at 496. From these comments, made in the context of a national fuel crisis, it is evident that

through COWPTA, Congress contemplated providing an incentive for the development of new technologies that would facilitate the production of alternative fuel sources. This view is reinforced by the House and Senate conference committee report, which states that "this provision is intended to provide producers of alternative fuels with protection against significant decreases in the average wellhead price for the uncontrolled domestic oil, with which alternative fuels frequently compete." H. Conf. Rep. No. 817, at 139, reprinted in 1980 U.S.C.C.A.N. 691.

This Committee Report statement also indicates Congress' intent to limit the credit given in Section 29 to crude oil substitutes, rather than domestic crude oil. At the time the statute was enacted, domestic crude oil was being produced in large amounts, by conventional recovery methods. *See* generally, S. Rep. No. 96-394 at 2, 1980 U.S.C.C.A.N. at 414; H.R. Rep. No. 96-304 at 4-7, 1980 U.S.C.C.A.N. at 591-94. For this reason, domestic crude oil would not logically be categorized as an alternative energy source. Congress believed that domestic crude oil production would be sufficiently stimulated by the presidential order lifting the price controls. H. Rep. No. 96-304 at 7, 1980 U.S.C.C.A.N. at 594. Therefore, Congress had no need to subsidize the production of domestic crude oil. Rather, it endeavored to credit the production of alternative fuels or so-called crude oil substitutes.

The definition of "tar sands" contained in the FEA Ruling is completely congruous with Congress' intent to both encourage the development of new technologies and limit the Section 29 credit to crude oil substitutes that could not be obtained using conventional methods. As previously

discussed, the Ruling was issued in response to inquiries regarding the scope of price controls and their application to synthetic fuels or crude oil substitutes. FEA Ruling 1976-4, 41 Fed. Reg. 25886 (1976). The Ruling holds that under the EPAA, the price controls only apply to those fuels in short supply. Id. Because crude oil substitutes, such as tar sand oil, were not being produced commercially either in 1973, when the EPAA was enacted, or in 1976, when the Ruling was issued, the Ruling concludes that Congress could not have intended the price controls to extend to those crude oil substitutes. *Id.*

Thus, the FEA Ruling excludes from the definition of tar sands any crude oil that was being commercially produced at the time. The Ruling characterizes tar sands as

> the several rock types that contain an extremely viscous hydrocarbon which is not recoverable in its natural state by conventional oil well production methods including currently used enhanced recovery techniques.

Id. This language clearly excludes oil recovered from conventional sources and, in turn, includes oil obtained from alternative sources. At the same time, it reflects the effort by Congress to promote the development of new technologies and new sources of oil recovery. Moreover, applying the FEA definition to Section 29 and thereby limiting the credit to oil not recoverable by conventional methods results in the exclusion of domestic crude oil from the credit. This, too, is consistent with Congress' intent in enacting Section 29 to provide a credit for the production of crude oil substitutes, rather than domestic crude oil.

In addition to its compliance with congressional intent, further support for the application of FEA Ruling 1976-4 to the Section 29 (Title II) definition of tar sands is found in Title I. In creating a tax on crude oil, Title I states that crude oil is to be defined according to "the June 1979 energy [(EPAA)] regulations." 26 U.S.C. § 4996(b) (repealed 1988). Numerous other statutory terms in Title I also refer to the June 1979 energy regulations. *See, e.g.*, 26 U.S.C. §§ 4991(d)(1)(a), (e)(2), 4993 (b)(1), (b) (2), (c)(1)(A). In addition, the Report of the Senate Committee on Finance states that "it is anticipated that the Secretary will give due consideration to the various administrative rulings and judicial decisions which have interpreted or which construe [the energy] regulations." S. Rep. No. 96-394 at 57, 1980 U.S.C.C.A.N. at 466-67. All of these factors indicate Congress' intent that the regulations and rulings promulgated by the FEA under the EPAA be applied to COWPTA.

These references in Title I and in the legislative history to FEA regulations and rulings take on special significance when viewed in the context of the Act as a whole. Title I, which creates the tax on crude oil, and Title II, which grants a credit for oil derived from alternative sources, are both pieces of a comprehensive, integrated statutory scheme directed toward addressing the energy crisis of the late 1970's. The substantial link between the two statutes is evidenced by Congress' indication that the revenue derived from the Title I tax would serve to fund energy programs enacted under COWPTA. H. R. Rep. No. 96-304 at 4, 1980 U.S.C.C.A.N. at 591; S. Rep. No. 96-394 at 8, 1980 U.S.C.C.A.N. at 419. In light of this unified statutory scheme, it is both reasonable and appropriate to extend to Title II a definition contained in an administrative ruling directly applicable to Title I.

Shell argues that it is incorrect to apply Ruling 1976-4 to define "tar sands" for the purpose of Section 29. First, Shell argues that the Government's position incorrectly assumes that the EPAA and Section 29 tax credit are *in pari materia*. (D.I. 342 at 65). Shell argues that broad references to the same subject matter are insufficient to support *in pari materia* reading of statutes. (D.I. 342 at 67) On this point, Shell contends that while EPAA and Section 29 both deal with the subject of oil production generally, their particular purposes are completely opposite. Shell asserts that the FEA Ruling defines tar sands pursuant to the EPAA, not COWPTA. (D.I. 342 at 66). Shell argues that the EPAA created price ceilings on domestic oil in order to decrease production, whereas COWPTA was part of an effort to lift the price controls in order to increase domestic oil production. (D.I. 342 at 66). Therefore, because the EPAA and COWPTA had opposite purposes, Shell argues that the two statutes cannot be read in pari materia. (D.I. 342 at 67). As a result, Shell asserts that the FEA Ruling, promulgated under the EPAA, does not extend to COWPTA. (D.I. 342 at 67).

The Court finds this argument unpersuasive. Under the doctrine of *in pari materia*, statutes relating to the same subject matter should be construed together. Black's Law Dictionary 791 (1990); *see Erlenbaugh v. United States*, 409 U.S. 239, 243-44, 34 L. Ed. 2d 446, 93 S. Ct. 477 (1972). However, regardless of whether the EPAA and COWPTA address the same subject matter, Shell 's reasoning disregards the direct references made in the WPT to the applicability of the June 1979 energy regulations, as well as the statements in the legislative history indicating that guidance for interpreting COWPTA should be sought in administrative regulations and rulings. The *in pari materia* doctrine need not be applied in

order to perceive Congress' intent that the energy regulations be applied to COWPTA.

Along the same lines, Shell argues that even if the FEA Ruling is applicable to the Windfall Profit Tax, the tax and the Section 29 credit are not *in pari materia*, and therefore, the FEA Ruling does-not extend to Section 29. The Court is not convinced by this argument. The WPT and Section 29 are parts of the same act. The legislative history of COWPTA clarifies the link between them and provides a historical context that solidifies the connection. Because the Court finds the WPT and Section 29 to be *in pari materia*, the meaning of Section 29 may be gathered from the legislative intent supporting the WPT. *Dillon, Read & Co. v. Commercial State Bank*, 62 F.2d 606, 608 (3d Cir. 1932).

Finally, Shell argues that the phrase "currently used enhanced recovery techniques," which is used in the FEA Ruling, is ambiguous and unworkable because technology is constantly changing. Again, the Court must refer to the principle that a statute's meaning is to be construed at the time of its enactment. *McDermott*, 498 U.S. at 342. Thus, the point of reference for determining what constitutes a "currently used enhanced recovery technique" would be the time at which Section 29 was enacted.

For all of these reasons, the Court finds the FEA Ruling definition of tar sands to be applicable to Section 29. With this established, the Court will now address its concerns with the industry definition proposed by Shell.

B. Shell's Proffered Definition

Instead of the FEA Ruling definition, Shell seeks to apply an industry definition under Section 29. This definition characterizes tar sands as:

> Any consolidated or unconsolidated rock (other than coal, oil shale, or gilsonite) that either:
>
> (1) contains a hydrocarbonaceous material with a gas-free viscosity, at original reservoir temperature, greater than 10,000 centipoise, or (2) contains a hydrocarbonaceous material and is produced by mining or quarrying.

(D.I. 342 at 23-24). The definition, which Shell contends is based upon a general consensus in the petroleum industry, focuses on viscosity as the pivotal factor in categorizing oil as tar sand oil. The Court finds the Viscosity Standard to be problematic for several reasons.

1. Hindsight Analysis

The testimony offered at trial suggests that, in fact, there was no industry consensus regarding a definition for tar sands in 1980 when Section 29 was enacted. Shell's own expert, Dr. Aziz, conceded this point in his testimony, and Shell reiterates this concession in its Proposed Findings of Fact. (D.I. 307,
Aziz at 86; D.I. 342 at 30, P 102).

In addition, Dr. Aziz testified that a consensus developed in 1983, a full three years after Section 29 was enacted. (D.I.

307, Aziz at 88). In framing this consensus, Shell cites numerous agencies and organizations that approved the Viscosity Standard between 1980 and 1987. (D.I. 342 at 30, ¶ 102).

By asking the Court to apply to a 1980 statute a definition that did not come to fruition until 1983, Shell is advocating a hindsight analysis. It is axiomatic that a court must interpret a statute according to its meaning at the time it was enacted, not at some randomly-selected future time. *McDermott*, 498 U.S. at 342; *Perrin v. United States*, 444 U.S. 37, 42, 62 L. Ed. 2d 199, 100 S. Ct. 311, *cert. denied*, 444 U.S. 990 (1979). Thus, even if Shell had demonstrated a consensus regarding the Viscosity Standard, the fact that it arose three years after Section 29 was enacted prevents the Court from applying the Viscosity Standard to Section 29.

To this same end, Shell provided evidence at trial of an Internal Revenue Service final draft regulation that used the Viscosity Standard to define tar sands. (PX 208, Exh. A). The parties stipulated that the draft was approved by the Director of the Legislation and Regulations Division of the IRS and circulated for final signatures. (PX 208, ¶ 3). The draft is dated November 3, 1986. (PX 208, Exh. A). Of course, the draft regulation is entitled to little, if any, weight in the Court's analysis because it never received final administrative approval and therefore was never enacted. (*See* PX 208, ¶ 4). Additionally, the draft is a 1986 document and not contemporaneous with the enactment of Section 29. In the Court's view, these two factors render the draft regulation of little value in the Court's task of interpreting the language of Section 29 at the time it was enacted in 1980.

2. Contradictions With Congressional Intent

Additionally, the Court finds Shell's definition to be contrary to Congress' intent in enacting Section 29. As discussed previously, both the title and the legislative history of Section 29 indicate that the credit applies to fuel from an alternative source. Shell's definition focuses on the type of fuel, rather than its source, which is incompatible with Congress' intentions. Furthermore, application of the Viscosity Standard advocated by Shell would require tar sands to be defined differently under Title I and Title II, a result which Congress clearly did not intend. An explanation of this problem requires an review of the definitions contained in COWPTA.

Title I of COWPTA imposed an excise tax (the WPT) on domestically produced "crude oil." 26 U.S.C. §§ 4986(a), 4991(a) (repealed 1988). "Crude oil" included "heavy oil" and "incremental tertiary oil." 26 U.S.C. §§ 4991(e)(1) (repealed 1988). "Heavy oil" was defined as all crude oil produced from a property with a weighted average gravity of 16 API or less. 26 U.S.C. § 4991(e)(3)(B) (repealed 1988). "Incremental tertiary oil" was defined as the excess of crude oil removed from a property during the period for which a qualified tertiary recovery project was in effect over the base level of crude oil removed from a property. 26 U.S.C. § 4993(a) (repealed 1988). A "qualified tertiary recovery project" included those methods described in Section 212.78 of the Mandatory Petroleum Price Regulations as of June 1979. 26 U.S.C. § 4993(d)(1)(A) (repealed 1988). Among

these methods were "steam drive injection"[3] and "cyclic steam injection," both of which were used by Shell to recover oil in the Potter Sands.[4] 10 C.F.R. 212.78 (1979); (DX 897).

In the legislative history of Title I, Congress described crude oil as excluding "synthetic petroleum such as oil produced from . . . tar sands." S. Rep. No. 96-394 at 56, 1980 U.S.C.C.A.N. at 465. Thus, Congress explicitly distinguished crude oil from tar sands, and understood tar sands to be a crude oil substitute.

Applying these definitions, oil meeting Shell's Viscosity Standard, i.e., high-viscosity oil produced by enhanced

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[3] Steam injection involves the cyclic application of steam, also known as steam soak, steam stimulation or steam "huff and puff." (D.I. 296 at ¶ 24).). In the process, steam is injected down a well, and the well is shut-in. The steam remains in the reservoir, transferring its thermal energy to the oil and reservoir rock, reducing the oil's viscosity and allowing the oil to flow more freely toward the wellbore. (*Id.*).

[4] In 1963, Shell began using steam injection technology to recover oil on the Shell Mineral Properties. (D.I. 296 at 9, ¶ 24). Steam injection technology has been used as a recovery technique in the petroleum industry for thirty to forty years. (D.I. 342 at 11); (D.I. 306, Aziz Vol. A at 72). Shell began using cyclic steam technology in 1959 in Venezuela, and also used the process in California beginning in 1960. (D.I. 313, Hite at 108); (D.I. 334, Def. FF # 52). The use of steam injection technology grew rapidly in the petroleum industry and by 1967, cyclic steam techniques were producing an estimated 120,000 barrels of oil per day. (D.I. 313, Blevins at 109).

recovery methods such as steamsoak or steamflood,[5] would constitute heavy oil and incremental tertiary oil for the purposes of the WPT. Consequently, it would be taxed as crude oil and, therefore, excluded from the category of tar sands. That same oil, however, would be defined as tar sands under Section 29 according to Shell's definition. This would result in two different definitions of tar sands under Title I and Title II. Clearly, this was not the intent of Congress. *See Stockholms Enskilda Bank*, 293 U.S. at 87 (same words in different parts of same act are intended to have same meaning).

Moreover, under Shell's definition, the same oil would be subject to both a tax and a credit. Absent some evidence that Congress intended such an anomalous result, the Court cannot adopt such a position.

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[5] In steamflood, steam is injected into the reservoir through dedicated injection wells. (*Id.* at ¶ 58). Steamflood differs from cyclic steam methods in that steam is continuously injected into the injection well. (*Id.*). The steam enters the oil bearing area and creates a heated zone that generally forms at the top of the reservoir. This heated zone extends from the injecting well to one or more oil producing wells. The heated crude oil then flows from the heated zone to the production well, where it is pumped to the surface. (*Id.*); (D.I. 313, Blevins at 112-113).

In 1971, Shell began employing a steam drive or steamflood process on its California properties. (D.I. 334, at ¶ 57). Beginning in the early 1970's, the petroleum industry began to apply the steamflood recovery process on a large scale. (D.I. 334 at ¶ 60). By 1980, production from steamflood in California was more than 100,000 barrels of oil per day. (*Id.*).

C. The Tax Court Opinion

Application of the FEA Ruling definition as opposed to the Viscosity Standard definition is reinforced by the United States Tax Court's decision in *Texaco Inc. v. Commissioner of Internal Revenue*, 101 T.C. 571 (1993). While not binding on this Court, the identical issue is addressed and the Tax Court's reasoning is instructive.

In *Texaco*, the Tax Court was asked to define "oil produced from ... tar sands " under 26 U.S.C. § 29. 101 T.C. at 572. Relying exclusively on the language of the statute and an examination of its legislative history, the Tax Court concluded that Congress intended the FEA Ruling definition of tar sands to apply to Section 29. *Id.* at 576.

The Tax Court determined that Section 29 was enacted to encourage the development and production of alternative sources of crude oil. *Id.* at 575. In making this determination, the Tax Court noted that the legislative history of the WPT, Title I of COWPTA, explicitly states that crude oil, to which the WPT applied, included only natural crude petroleum and did not include synthetic petroleum such as oil produced from tar sands. *Id.* at 579 (citing S. Rep. No. 96-394, at 56 (1979), H. Conf. Rep. 96-817, at 114 (1980)). Based on its examination of the legislative history, the Tax Court concluded that Congress understood oil produced from tar sands to be a crude oil substitute and not simply a type of high viscosity crude oil. *Id.*

The Tax Court further noted that the Viscosity standard definition proposed by Texaco would require the term "tar sands" to have different meanings for purposes of Title I and

Title II. *Id.* at 580. Stating that Congress would not have used the same term in fundamentally different ways within the same legislative enactment without clearly expressing an intent to do so, the court declined to adopt the plaintiff's proposed definition. *Id.* (*citing Helvering v. Stockholms Enskilda Bank*, 293 U.S. 84, 87, 79 L. Ed. 211, 55 S. Ct. 50 (1934)). Therefore, the Tax Court held that the FEA Ruling definition of tar sands was applicable to Section 29.

Shell argues that *Texaco* is not binding precedent on this Court and that its influence is dependent upon the persuasiveness of its reasoning. (D.I. 342 at 59). Shell further argues that the Tax Court's reasoning in Texaco was flawed because the court misconstrued oil produced from tar sand as synthetic oil. (D.I. 255 at 33).

More specifically, Shell asserts that oil produced from tar is a form of crude oil and is not synthetic oil. (D.I. 255 at 34). In support of this position, Dr. Aziz testified that within the petroleum industry the phrase "oil produced from tar sand" means an extremely viscous crude oil produced from tar sand. (D.I. 306 at 47). Dr. Aziz testified that oil is made of hydrogen and carbon and as the fraction of carbon increases, the oil becomes more viscous. (D.I. 306 at 46). Dr. Aziz further testified that oil produced from tar sand is extremely viscous, but can be upgraded to synthetic oil through a process whereby either hydrogen is added or carbon is removed from the oil. (D.I. 306 at 46). Consequently, only through the process of upgrading is oil produced from tar sands converted into synthetic oil. Therefore, Shell argues that the *Texaco* case should be given little or no weight by this Court because the Tax Court misconstrued oil produced from tar sands as synthetic oil. (D.I. 255 at 32-24).

The Court is not convinced. Shell advances this argument in an apparent attempt to divorce Title II from Title I and its informative legislative history and thereby render the FEA Ruling inapplicable to COWPTA. As previously discussed, defining tar sand oil as crude oil, rather than synthetic, would allow Shell to advance the theory that it is consistent to subject the same oil to the WPT and the Section 29 credit, and therefore, there is no connection between the two. However, the legislative history reveals that Congress viewed tar sand oil as a type of synthetic oil, as distinguished from crude oil. H. Rep. No. 96-394 at 56 (stating that crude oil "does not include synthetic petroleum, such as oil from . . . tar sands."). Therefore, in this Court's view, the Tax Court properly characterized tar sand oil as synthetic, and applied the FEA Ruling to Section 29 appropriately.

VII. CONCLUSION

For the reasons discussed, the Court concludes that the FEA Ruling definition is the proper definition to be applied in construing Section 29 of COWPTA.[6]

An Order consistent with this Memorandum Opinion will be entered.

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[6] As agreed by the parties, because the Court has applied the FEA Ruling definition to Section 29, the Court will not address the means by which Shell applied its Viscosity Standard.

FINAL JUDGMENT ORDER

WHEREAS, the Court held a bench trial on the merits of this case in August and September, 1995;

NOW THEREFORE, IT IS HEREBY ORDERED AND ADJUDGED this 16th day of October, 1997, that, for the reasons set forth in the Memorandum Opinion issued this date, JUDGMENT is entered in favor of the DEFENDANT, the United States of America.

/s/_____
Joseph J. Farnan, Jr.
UNITED STATES DISTRICT JUDGE